No. 86-998 (1)

IN THE

Supreme Court of the United States

October Term, 1986

JAPAN AIR LINES COMPANY, LTD.
and
SWISSAIR, SWISS AIR TRANSPORT
COMPANY, LTD.,
Petitioners,

v.

ELIZABETH HANFORD DOLE,
Secretary of Transportation,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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December 18, 1986

CASILLAS PRESS INC. – 1717 K STREET NW WASHINGTON DC 20037 – 223-1223

QUESTIONS PRESENTED

1. Was the Civil Aeronautics Board required to apply the flow of commerce doctrine which looks to the essential character of the transportation and the intent of the shipper, as established by this Court in *Texas & N.O.R.R. v. Sabine Tram Co.,* 227 U.S. 111 (1913), *Baltimore & O.S.W.R.R. v. Settle,* 260 U.S. 166 (1922) and related cases, in determining whether a Chicago-Seattle air cargo rate, which could only be used in conjunction with international transportation between Seattle and a point in a foreign country, was a rate applicable to foreign air transportation?

2. Did the Court of Appeals err in failing to require the C.A.B. to provide a reasoned analysis of its abandonment of this Court's flow of commerce doctrine which the agency had consistently applied in prior decisions?

LIST OF PARTIES

Petitioners in this case are:

Japan Air Lines Company, Ltd. and
Swissair, Swiss Air Transport Company, Ltd.

No parents, subsidiaries, or affiliated companies are publicly traded in the United States or otherwise owned in any measure by United States citizens.

Respondent in this case is:

Elizabeth Hanford Dole,
Secretary of Transportation

Additional parties:

The following were also parties or intervenors in the Court of Appeals:

Lufthansa German Airlines
Pan American World Airways, Inc.
Trans World Airlines, Inc.
Northwest Airlines, Inc.
British Airways, Plc.

TABLE OF CONTENTS

Page

QUESTIONS PRESENTED i

LIST OF PARTIES ii

TABLE OF AUTHORITIES v

OPINIONS BELOW 1

JURISDICTION 2

STATUTES AND TREATIES INVOLVED IN THE CASE 2

STATEMENT OF THE CASE 2

REASONS FOR GRANTING THE WRIT 5

I. The C.A.B. Decision Is Contrary To and Inconsistent With Supreme Court Precedent and Federal Appellate Court Decisions 6

II. The Court of Appeals Erred in Failing to Apply the Requisite Degree of Scrutiny to the C.A.B. Decision Substituting the Newly Created Carrier-Restricted Test for the Long Established Essential Character/Flow of Commerce Test 14

CONCLUSION 18

APPENDIX A 1a

APPENDIX B 23a

APPENDIX C 93a

APPENDIX D 155a

Page

APPENDIX E 161a

APPENDIX F 163a

TABLE OF AUTHORITIES

Page

Supreme Court Cases:

Baltimore & O.S.W.R.R. v. Settle, 260 U.S. 166 (1922) . . . . *passim*

Illinois Central R.R. v. De Fuentes, 236 U.S. 157 (1915) 8

Illinois Natural Gas Co. v. Central Illinois Public Service Co., 314 U.S. 498 (1942) 13

McElroy v. United States, 455 U.S. 642 (1982) 8

Motor Vehicle Manufacturers Ass'n v. State Farm Mutual Insurance Co., 463 U.S. 29 (1983) 14

Texas & N.O.R.R. v. Sabine Tram Co., 227 U.S. 111 (1913) . . . . *passim*

United States v. Capital Transit Co., 325 U.S. 357 (1945) 7-8

United States v. Erie R.R., 280 U.S. 98 (1929) 7, 11, 13

Other Federal Cases:

Greater Boston Television Corp. v. FCC, 444 F.2d 841 (D.C. Cir. 1970), *cert. denied*, 403 U.S. 923 (1971) 6, 14

Japan Air Lines Co. v. Dole, 801 F.2d 483 (D.C. Cir. 1986) 1, 5, 15-17

NAACP v. FCC, 682 F.2d 993 (D.C. Cir. 1982) 14

Page

United States v. Cassaro, Inc.,
443 F.2d 153 (5th Cir. 1971) 13

United States v. Maddox,
394 F.2d 297 (4th Cir. 1968) 8

Administrative Cases:

Agreement Between South Thailand and the United States,
Initial Decision, 10 F.M.C. 201, *adopted*, 10 F.M.C.
199 (1966) 12

Air Florida-BIA Wet Lease,
102 C.A.B. 730 (1983) 11

Air Freight Forwarders, Revocations,
65 C.A.B. 1605 (1974) 10

Application of Air Tungaru-UTA,
90 C.A.B. 606 (1981) 10

Armstrong World Industries, Inc.,
No. MC-C-10963 (I.C.C. April 3, 1986) 12

Canadian Colonial Airways, Inc. - Investigation,
2 C.A.B. 752 (1941) 10-11, 16

Eastern Air Lines, Inc., Enforcement Proceeding,
40 C.A.B. 745 (1964) 11, 17

Intercoastal Investigation,
1 U.S.M.C. 400 (S.B.B. 1935) 12

*Iron and Steel Articles from Wilmington, North
Carolina to Points in North Carolina via General
Motor Lines, Inc.*, 323 I.C.C. 740 (1965), *aff'd sub nom.
North Carolina Utilities Commission v. United States*,
253 F. Supp. 930 (E.D.N.C. 1966) 11

Page

Resort Airlines Miami Stopover Investigation, 19 C.A.B. 1 (1954) 10, 16

Restrictions on Transshipment at the Canal Zone, 2 U.S.M.C. 675 (1943) 12

Southern States Cooperative v. Baltimore & O.R.R., 323 I.C.C. 400 (1964) 11-12

Visit USA Fare/Export Inland Contract Rate Investigation, Initial Decision, C.A.B. Docket No. 40269 (ALJ June 3, 1983) 2-3, 5, 8-9

Visit USA Fare/Export Inland Contract Rate Investigation, Opinion and Order on Discretionary Review, Order No. 84-8-55 (C.A.B. 1984) 2-4, 15-18

Statutes and Regulations:

Airline Deregulation Act of 1978, as amended, Section 1601, 49 U.S.C. §1551 5

Civil Aeronautics Act of 1938, ch. 601, Section 1(21), 52 Stat. 973 10

Federal Aviation Act of 1958, as amended,
Section 101(24), 49 U.S.C. §1301(24) . . . . *passim*
Section 403, 49 U.S.C. §1373 . . . . 2-3, 7
Section 1006(a), 49 U.S.C. §1486(a) 5
Section 1102, 49 U.S.C. §1502 . . . . 2, 7

Shipping Act, 1916, ch. 451, 39 Stat. 728 (codified as amended at 46 U.S.C. §§801-842) 12

Shipping Act of 1984, as amended,
Section 3(6), 46 U.S.C. §1702(6) 13
Section 4, 46 U.S.C. §1703 13
Section 8, 46 U.S.C. §1707 13

Page

28 U.S.C. §1254(1) 2

14 C.F.R. §572.104(ff) 13

Treaties:

Annex to the United States-Switzerland Air Transport Services Interim Agreement of 1945, May 13, 1949, Section VII, 63 Stat. 2437, T.I.A.S. No. 1949 . . . . 2-3, 7

United States-Japan Air Transport Services Agreement of 1952, Art. 13, 4 U.S.T. 1948, T.I.A.S. No. 2854 . . . . 2-3, 7

Miscellaneous:

46 Fed. Reg. 46, 787 (1981) 17-18

50 Fed. Reg. 6944 (1985) 13

IN THE

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v.

ELIZABETH HANFORD DOLE,
Secretary of Transportation,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Japan Air Lines Company, Ltd. and Swissair, Swiss Air Transport Company, Ltd. respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit entered in this case on September 19, 1986.

OPINIONS BELOW

The opinion of the Court of Appeals appears in Appendix A to this Petition, and is reported at 801 F.2d 483.

Civil Aeronautics Board Order 84-8-55 appears in Appendix B and the Initial Decision of Administrative Law Judge John M. Vittone appears in Appendix C.

JURISDICTION

The judgment of the Court of Appeals was entered on September 19, 1986. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

STATUTES AND TREATIES INVOLVED IN THE CASE

The statutory provisions involved in this case are Sections 101(24), 403(a) and 1102 of the Federal Aviation Act of 1958, as amended, codified at 49 U.S.C. §§1301(24), 1373(a) and 1502 (Appendix D). This case also involves the United States-Japan Air Transport Services Agreement, August 11, 1952, Art. 13, 4 U.S.T. 1948, 1954, T.I.A.S. No. 2854 (Appendix E) and the Annex to the United States-Switzerland Air Transport Services Interim Agreement of 1945, May 13, 1949, Section VII, 63 Stat. 2437, T.I.A.S. No. 1949 (Appendix F).

STATEMENT OF THE CASE

This case originated upon the filing of a complaint with the Civil Aeronautics Board ("C.A.B." or "the Board") on October 27, 1980 by the Petitioners and other foreign airlines against the "Visit U.S.A." or "VUSA" fares of certain U.S. air carriers.[1] On May 4, 1981, Japan Air Lines Com-

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[1] In addition to the Petitioners, Lufthansa German Airlines, Philippine Airlines, Inc., and Singapore Airlines Limited were parties to the original complaint.

pany, Ltd. filed a complaint against the "Export Inland Contract Rates" of Northwest Airlines, Inc. ("Northwest"). The Export Inland Contract rates were rates, which although applicable to transportation of cargo between Chicago and Seattle, could only be used in conjunction with international transportation beyond Seattle to a point in Japan or other points in the Orient. The complaints alleged, *inter alia,* that the Export Inland Contract rates constituted rates in "foreign air transportation" which were subject to the tariff filing requirements of the Federal Aviation Act of 1958, as amended, 49 U.S.C. §1301 *et seq.*, ("the Act") and relevant bilateral Civil Air Transport Agreements.[2]

On December 1, 1981, the C.A.B. instituted an investigation to determine, *inter alia,* whether the Export Inland Contract rates should be classified as domestic or international under the Act and the relevant bilateral agreements.

On June 3, 1983, after a full oral evidentiary hearing, the C.A.B.'s Administrative Law Judge ("ALJ") issued his Initial Decision (Appendix C). The ALJ analyzed the essential character of the Export Inland rates and found, *inter alia,* that ". . . there is little doubt that the Export-Inland Contract rates are rates in foreign air transportation." (Appendix C, page 146a.) Accordingly, he also found, pursuant to Section 403(a) of the Act, and the relevant bilateral Air Transport Agreements, that they were required to be filed in tariffs with the C.A.B. and with foreign aeronautical authorities.

After granting discretionary review of the Initial Decision, the C.A.B. issued Order 84-8-55, adopted on August

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[2]The C.A.B. decision relating to the VUSA fares was not appealed by Petitioners to the Court of Appeals and is not at issue.

10, 1985. In that order, the Board reversed the ALJ's finding that the Export Inland rates were rates in foreign air transportation. In determining that the rates were domestic the Board explicitly rejected the "flow of commerce" test and instead created a new "carrier-restricted" test which it applied in this case.

The term "carrier-restricted test" simply means that an export rate will be classified as either domestic or international depending *solely* on whether the carrier offering the rate explicitly *restricts* its availability only to those shippers who agree in advance to use the transportation services of the offering carrier over both the international as well as the domestic sector. If the rate is so restricted, it is an international rate. If it is not so restricted, it is irrelevant whether the same carrier actually and invariably provides the transportation over both the domestic sector and the international sector since in either case the C.A.B. would classify that rate as domestic. It is only when the offering carrier explicitly restricts the availability of the export rate to shipments which are carried on its own international services — and the rate is thus "carrier restricted" — that the rate is classified as an international rate.

Applying this test to Northwest's Export Inland rates, which were available only for international shipments from Chicago to Seattle which continued onward to points in the Far East, the C.A.B. classified these rates as domestic solely because Northwest did not explicitly restrict the availability of the rates to its own services. The C.A.B. classified these rates as domestic notwithstanding that (1) they were *not* available for purely domestic shipments originating in Chicago and terminating in Seattle nor for any other *solely* domestic transportation and (2) *all* of the shipments which used the Export Inland Con-

tract rates were transported by Northwest over both the Chicago/Seattle and the Seattle/Far East sectors *without any intervening break in the transportation.* (Appendix C, pages 146-150a.)

Pursuant to Section 1006(a) of the Act, 49 U.S.C. §1486(a), which confers jurisdiction to review orders of the Civil Aeronautics Board on the courts of appeals of the United States and the District of Columbia, Petitioners requested the United States Court of Appeals for the District of Columbia Circuit to review that part of the Board's decision which characterized the Export Inland Contract rate as a domestic rate. The Court of Appeals affirmed. (Appendix A.)

REASONS FOR GRANTING THE PETITION

This case raises the question of whether the C.A.B. erred in ignoring longstanding Supreme Court precedent by abandoning the essential character/flow of commerce doctrine, which it had previously applied in a uniform fashion, in determining that a Seattle-Chicago air cargo rate which could only be used in conjunction with transportation from Seattle to a point in a foreign country was not a rate applicable to foreign air transportation.[3] The C.A.B.'s refusal to apply the essential character/flow of commerce doctrine and its replacement by a newly created carrier-restricted test to determine the nature of a movement in transportation is inconsistent with the holdings of

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[3]Less than five months following its decision in this case the C.A.B.'s regulatory responsibilities were transferred to the U.S. Department of Transportation pursuant to Section 1601 of the Airline Deregulation Act of 1978, 49 U.S.C. §1551. For purposes of simplicity, we will use the term C.A.B. as referring to both the Civil Aeronautics Board and the Department of Transportation.

this and numerous other courts. It is also inconsistent with the practice of the courts and the federal administrative agencies in differentiating between domestic and intrastate commerce on the one hand, and foreign and interstate commerce on the other hand. Accordingly, grant of this petition is required to (1) reaffirm the applicability and vitality of this Court's essential character/flow of commerce doctrine, (2) eliminate the conflicts between the various U.S. Appellate Circuits created by the Court of Appeals decision in this case and (3) prevent the C.A.B. from arbitrarily abandoning its longstanding policy of applying this Court's essential character doctrine without the required "reasoned analysis, indicating that prior policies and standards are being deliberately changed, not casually ignored. . . ." *Greater Boston Television Corporation v. Federal Communications Commission,* 444 F.2d 841, 852 (D.C. Cir. 1970), *cert. denied,* 403 U.S. 923 (1971).

I. The C.A.B. Decision Is Contrary To and Inconsistent With Supreme Court Precedent and Federal Appellate Court Decisions

This case is the result of the C.A.B. reversal of its ALJ's Initial Decision which found that the Export Inland Contract rates established by Northwest constituted cargo rates in foreign air transportation within the meaning of Section 101(24) of the Act. Section 101(24) defines foreign air transportation as

> the carriage by aircraft of persons or property as a common carrier for compensation or hire or the carriage of mail by aircraft, in commerce between . . . a place in the United States and any place outside thereof; whether such commerce moves wholly by aircraft or partly by aircraft and partly by other forms of transportation.

Pursuant to Section 403(a) of the Act, 49 U.S.C. §1373(a) all foreign and U.S. carriers, including the Petitioners and Northwest, are required to file tariffs with the C.A.B. for all cargo rates in foreign air transportation. In addition, the bilateral agreements governing foreign air transportation require that all fares and rates for transportation between the United States and the applicable foreign country be filed with each nation's aeronautical authority.[4] In this connection, Section 1102 of the Act, 49 U.S.C. §1502, obligates the C.A.B. to act consistently with "any obligation assumed by the United States in any treaty, convention, or agreement that may be in force between the United States and any foreign country or foreign countries . . . ." (Appendix D, pages 159a-160a.)

It is axiomatic that "the essential character of the commerce" is the decisive test in resolving the status of a particular movement, *Texas & N.O.R.R. v. Sabine Tram Co.*, 227 U.S. 111, 126 (1913), and that the shipper's intent determines the essential character of the commerce. *Baltimore & O.S.W.R.R. v. Settle,* 260 U.S. 166, 170-171 (1922). *Accord United States v. Erie R.R.*, 280 U.S. 98 (1929) (rail transportation of wood pulp from port through which imported to point in same state held part of foreign commerce); and *United States v. Capital Transit Co.*. 325 U.S. 357 (1945) (bus transportation between two points within the District of Columbia held to be within in-

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[4]*E.g.*, Annex to the United States-Switzerland Air Transport Services Interim Agreement of 1945, May 13, 1949, Section VII, 63 Stat. 2437, T.I.A.S. No. 1929; United States-Japan Air Transport Services Agreement of 1952, Art. 13, 4 U.S.T. 1948, 1954, T.I.A.S. No. 2854 (Appendices E and F).

terstate commerce to the extent it involved passengers whose journey originated or ended in Virginia).[5]

The ALJ, who was the initial C.A.B. decisionmaker, found that the Export Inland Contract rates constituted rates in foreign air transportation which must be filed with the United States and relevant foreign governments. In arriving at that conclusion, the ALJ relied on the traditional essential character analysis, stating that:

- ". . . the intent and effect of the contract rates was to enhance Northwest's competitive position in an international market." (Appendix C, page 147a.)
- "The contracts state that the 'rates are applicable *only to international shipments* which terminate in . . . Hong Kong, Japan, South Korea, Philippines, or Taiwan.' " (*Id.;* emphasis added by ALJ.)
- "The contract also requires that the domestic air bill covering the movement from Chicago to Seattle include a signed endorsement that the

[5]*See also* Illinois Central R.R. v. De Fuentes, 236 U.S. 157, 163 (1915) (when "interstate character has been acquired it continues, at least, until the load reaches the point where the parties originally intended that the movement should finally end."); *Compare* McElroy v. United States, 455 U.S. 642, 652-653, 658 (1982) (in drafting a statute prohibiting the interstate transportation of forged securities, Congress intended the term "interstate commerce" to be as broad in scope as the Court's longstanding decisions holding that such "commerce begins well before state lines are crossed, and ends only when movement of the item in question has ceased in the destination State."); *compare also* United States v. Maddox, 394 F.2d 297, 299-300 (4th Cir. 1968) (removal of stolen sugar to a warehouse was a mere interruption in the flow of commerce which did not destroy interstate character of the shipment for purposes of establishing federal criminal jurisdiction).

shipment is a '*true international* shipment beyond the [Seattle] gateway.' " *(Id.)*

- "[A]n internal Northwest document . . . states that the rate is to be used for 'transpacific rate construction purposes.' " (*Id.*)
- "Northwest's witness conceded that the rate was instituted to meet competition in the movement of international cargo from Chicago to the Orient." (*Id.* at page 148a.)

Significantly, the ALJ's reliance on the essential character of the rates is consistent with the C.A.B.'s directive to the parties to introduce:

> comprehensive factual evidence as to whether these fares as actually applied are typically part of a continuous integrated international journey originating and terminating in a foreign country. . . .

(Appendix C, page 109a, *quoting from* C.A.B. Order 81-11-182 at 8.) This directive evidences that the C.A.B. at least when instituting its investigation, intended to conform to the essential character/flow of commerce doctrine to determine the status of the Export Inland rates. Nonetheless, it summarily dismissed its own fact finder's determination which was consistent with that doctrine. Instead, it created an entirely new "carrier-restricted" test, effectively reversing its own precedents as well as those established by this Court and consistently applied by other federal courts and federal administrative agencies.

Other than in the instant case, the C.A.B. has adhered to judicial precedent and repeatedly looked to the essential character of the transportation provided and the intent of the passenger or shipper in differentiating between domestic and foreign air transportation. As early as 1941 it cited

Settle, supra, and other essential character/flow of commerce cases and stated that:

> These cases furnish a *controlling* analogy for determining whether the carriage here involved is "foreign air transportation" within the meaning of section 1(21).[6]

Canadian Colonial Airways, Inc. - Investigation, 2 C.A.B. 752, 754 (1941) (emphasis added) (transportation through U.S. airspace but between two foreign points did not constitute foreign air transportation notwithstanding an overnight stop at Jacksonville, Florida).

The C.A.B. reaffirmed its reliance on the essential character/flow of commerce doctrine in *Resort Airlines Miami Stopover Investigation,* 19 C.A.B. 1,9 (1954) (holding that the Miami to New York segment of a package tour involving travel beyond Miami to points in the Caribbean constituted foreign air transportation and explaining that it had undertaken an inquiry corresponding to that made in *Settle, supra,* where the "basic question posed by the court was the 'essential nature of the movement. . .' "); in *Air Freight Forwarders, Revocations,* 65 C.A.B. 1605, 1608 (1974) ("The Board has previously held that whether a shipment is moving in domestic or international air transportation is determined by its ultimate destination, and that a stopover which is merely an incidental part of a whole trip, does not affect this determination."); in *Application of Air Tungaru-UTA,* 90 C.A.B. 606 (1981) (service between two foreign points which would not otherwise be subject to U.S. jurisdiction held to be in foreign air

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[6]Section 1(21) of the Civil Aeronautics Act of 1938 (52 Stat. 973, 979) was recodified as, and is identical to, Section 101(24) of the Federal Aviation Act of 1958, as amended.

transportation and accordingly subject to U.S. jurisdiction because it constituted one segment of through service from a U.S. point to a foreign point); and in *Air Florida-BIA Wet Lease*, 102 C.A.B. 730 (1983) (". . . it is clear that the flights operated by [British Island Airways] will be part of a continuous operation by Air Florida between the United States and Amsterdam, Brussels, Dusseldorf, and Frankfurt. Such service is clearly in foreign air transportation and therefore subject to our jurisdiction and governed by our regulations." (Footnote *citing Canadian Colonial Airways, Inc., supra,* omitted.))[7]

Application of the essential character/flow of commerce doctrine extends beyond the field of aviation and has been followed in other regulatory settings. The Interstate Commerce Commission has *uniformly* looked to the essential character of the integrated movement to determine whether any individual segment is in foreign or interstate commerce. *See, e.g., Iron and Steel Articles from Wilmington, North Carolina to Points in North Carolina via General Motor Lines, Inc.*, 323 I.C.C. 740, 742, 744 (1965), *aff'd sub nom. North Carolina Utilities Commission v. United States,* 253 F. Supp. 930 (E.D.N.C. 1966) (*citing Settle, Erie* and *Sabine, supra,* for precept that "the essential character of the commerce determines whether a shipment is interstate (foreign) or intrastate in nature"; *Southern States Cooperative v. Baltimore &*

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[7]*See also* Eastern Air Lines, Inc., Enforcement Proceeding, 40 C.A.B. 745, 747 (1964) (where although the C.A.B. ultimately determined to dismiss the case and resolve the contested issues in another proceeding, it cited, *inter alia, Settle, supra,* and noted that "[a]s a general rule, the destination which was intended by the passenger when he begins the journey and which was known to the carrier and for which he purchased a ticket determines the character of the trip.").

O.R.R., 323 I.C.C. 400, 403-404 (1964) (inland shipments of imported merchandise were determined to be continuations of foreign commerce to which "import rate" tariffs applied, not as separate and distinct movements in domestic commerce, because the shipper's "intention . . . was to reship all inbound traffic in continuous movement."); *Armstrong World Industries, Inc.*, No. MC-C-10963, slip op. at 6-7 (ICC April 3, 1986) (*citing Settle* and *Sabine, supra,* for the propositions that "[i]t is well settled that characterization of transportation between two points in a State as interstate or intrastate in nature depends on the 'essential character' of the shipment" and that "[c]rucial to a determination of the essential character of a shipment is the shipper's fixed and persisting intent at the time of the shipment.").

The essential character test has also been used in tariff and rate situations by the Federal Maritime Commission and its predecessor agencies ("F.M.C."). For example, in *Intercoastal Investigation,* 1 U.S.M.C. 400, 440 (SBB 1935), the U.S. Shipping Board Bureau cited *Settle, supra,* and relied on the shipper's "original and continuing intention" to engage in intercoastal commerce by way of the Panama Canal for purposes of applying the tariff filing requirements of the Intercoastal Shipping Act. Similarly, the F.M.C. has held that carriers operating between two foreign ports and transshipping their cargo to United States bound carriers are part of the "continuous line" of carriage to the United States. Thus, the carriers were held to be common carriers engaged in foreign commerce under the Shipping Act of 1916. *Restrictions on Transshipment at the Canal Zone,* 2 U.S.M.C. 675, 679 (1943); *Agreement Between South Thailand and the United States,* Initial Decision, 10 F.M.C. 201, 209, *adopted,* 10 F.M.C. 199 (1966).

More recently, the F.M.C. amended its regulations to clarify that "[a]n agreement which involves movement of cargo in a domestic offshore trade as part of a through movement of cargo via transshipment involving the foreign commerce of the United States *shall be considered to be in the foreign commerce of the United States . . . .*" (46 C.F.R. §572.104(ff); emphasis supplied). Such agreements are therefore subject to the agreement and tariff filing requirements of the Shipping Act of 1984, which regulates common carriage by water in foreign commerce. 46 U.S.C. §§1702(6), 1703, 1707; *See* 50 Fed. Reg. 6944 (Feb. 19, 1985).[8]

Notwithstanding its own precedent dating back to at least 1941, the uniform practice of other federal administrative agencies, and the precedents of this and other federal courts, the C.A.B. arbitrarily abandoned the essential character/flow of commerce test in evaluating Northwest's Export Inland rate, and instead utilized a newly created "carrier-restricted test." The denial of this Petition would effectively sanction the new test and would undermine the existing, long established regulatory scheme based on the holdings in *Sabine, Settle,* and *Erie,*

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[8]The essential character/flow of commerce test has also been applied in the areas of natural gas pipeline regulation, *See* Illinois Natural Gas Co. v. Central Illinois Public Service Co., 314 U.S. 498, 503-504 (1942) (the "point at which the title and custody of the gas passes to the purchaser without arresting its movement to the intended destination does not affect the essential interstate nature of the business."); and the regulation of food and drugs, *see* United States v. Cassaro, Inc., 443 F.2d 153, 156 (5th Cir. 1971) (the Federal Food, Drug and Cosmetic Act contains "an overall scheme designed to regulate the interstate flow of goods 'from the moment of their introduction into interstate commerce' until 'the moment of their delivery to the ultimate consumer.' " *citing* United States v. Sullivan, 332 U.S. 689 (1948)).

supra, which currently pervades all aspects of commerce and transportation. Petitioners respectfully submit that the inconsistency of the new standard with the long established holdings of this Court justifies grant of this Petition.

II. The Court of Appeals Erred in Failing to Apply the Requisite Degree of Scrutiny to the C.A.B. Decision Substituting the Newly Created Carrier-Restricted Test for the Long Established Essential Character/Flow of Commerce Test

In reviewing the C.A.B. decision at issue here, the Court of Appeals failed to apply this Court's repeated holdings that there is a presumption against unexplained changes in agency policy. As stated in *Motor Vehicle Manufacturers Association v. State Farm Mutual Insurance Company*, 463 U.S. 29, 42 (1983):

> an agency changing its course . . . is obligated to supply a reasoned analysis for the change beyond that which may be required when an agency does not act in the first instance.

The Court of Appeals also ignored its holding that:

> an agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored. . . .

Greater Boston Television, supra, 444 F.2d at 852. Moreover, it failed to follow its admonition that agency deviation from established precedent necessitates a "heightened" scrutiny on review to ensure that the agency articulated permissible reasons for the change and that the new position is consistent with the law. *NAACP v. FCC*, 682 F.2d 993, 998 (D.C. Cir. 1982).

The C.A.B.'s abrupt abandonment of this Court's long established essential character/flow of commerce doctrine imposed a rigorous scrutiny requirement upon the Court of Appeals. It did not meet that requirement. To the contrary, the Court of Appeals utterly failed to investigate the nature and function of the Export Inland rate. Had it done so, it would have discovered that the C.A.B.'s freshly minted "test" has no rational basis. It is on its face unreasonable to classify an accurately labeled "Export" rate, which is available only to traffic destined to Japan and other points in the Far East beyond Seattle, but which is *not* available to purely domestic transportation, as a domestic rate. The fact that an export rate is not "carrier-restricted" does not affect its essentially foreign character when it can only be used in conjunction with international transportation. Petitioners respectfully submit that this Court should not sanction a "test" which leads to the arbitrary and illogical result that an export rate not available for domestic transportation is nonetheless classified as domestic.

Rather than remanding the decision to the C.A.B. for the "reasoned analysis" required by this Court, the Court of Appeals seized on the agency's self-serving statement that it had never unequivocally stated that the flow of commerce test is the *sole* test for determining whether air transportation is foreign. (Appendix A, page 9a.) As used by the C.A.B., that statement is apparently intended to signify that the agency has never unequivocally stated that all air transportation which arguably can be said to originate or terminate in a foreign country is automatically foreign air transportation. (Appendix B, page 56a.) The Court of Appeals apparently accepted the C.A.B.'s characterization of Petitioners' argument as advocating an extreme "strict" flow of commerce test which would mandate

that any nexus, no matter how remote, to foreign commerce is sufficient to categorize a movement as foreign air transportation. This is a gross mischaracterization of Petitioners' position. Petitioners argue only that the C.A.B. must adhere to this Court's repeatedly stated requirement that an agency look to the essential character of the transportation and to the intent of the shippers in determining whether the transportation is foreign or domestic.

The Court of Appeals' statement that "the CAB has never stated that the 'flow of commerce' test is the *sole* test for determining whether air transportation is foreign" (Appendix A, page 9a) is correct only insofar as it refers to the so-called "strict" flow of commerce test discussed above. Had the Court of Appeals more carefully examined C.A.B. precedent, it would have found that it manifests a consistent adherence to the essential character and shipper's intent criteria which underlie this Court's flow of commerce doctrine.

Thus, although *Canadian Colonial Airways, Inc. - Investigation,* 2 C.A.B. 752 (1941) does not state that the "flow of commerce" test is the *only* applicable test, it does, as the Court of Appeals notes, cite to *Settle, Sabine,* and other Supreme Court cases applying that test. Moreover, the C.A.B. clearly looked to the "essential character" of the Montreal-Nassau transportation at issue in that case in determining that an "incidental" stopover at Jacksonville, Florida did not transform what would otherwise be foreign air transportation into domestic air transportation.

Similarly, the C.A.B.'s failure to state that the "flow of commerce" test is the *only* applicable test in *Resort Airlines Miami Stopover Investigation,* 19 C.A.B. 1, 8 (1954) is irrelevant where it cited *Settle, supra,* as well as other

essential character/flow of commerce cases, and looked to the essential character of the transportation in framing the issue to be whether the stopover was "the principal or dominant part of the tour" such that "it seems apparent that the *essential nature* of the tour would be altered. . . ." (Emphasis added.)

Adherence to this Court's essential character/flow of commerce doctrine is also manifest in *Eastern Air Lines, Inc., Enforcement Proceeding,* 40 C.A.B. 745, 747 (1964). In that case, the agency cited *Settle, supra,* and said "[a]s a general rule, the destination which was intended by the passenger when he begins the journey and which was known to the carrier and for which he purchased a ticket determines the character of the trip."

Petitioners also disagree with the acceptance by the Court of Appeals of the C.A.B.'s assertion that the Board's *Tariff Flexibility Rulemaking,* 46 Fed. Reg. 46,787 (1981), is precedent for use of an alternative test. (Appendix A, pages 11a-12a.) This is patently incorrect. The *Tariff Flexibility Rulemaking* cannot reasonably be cited for anything other than continued C.A.B. reliance on the essential character/flow of commerce doctrine established by this Court. In rejecting the argument that any domestic fares and rates which could be combined with foreign fares or rates were actually fares in foreign transportation subject to tariff filing requirements, the C.A.B. obviously applied the essential character/flow of commerce test. The fares and rates in question were primarily domestic in nature and only incidentally combinable with fares and rates in foreign air transportation. The "essential character" of the fares and rates was domestic.[9] Accor-

[9]Significantly, the C.A.B. explicitly stated that the Export Inland rate is "distinguishable from the typical 'combinable' domestic fares which were the focus of the *Tariff Flexibility Rulemaking,* in that they

dingly, this rulemaking affirms rather than negates previous C.A.B. reliance on the essential character/flow of commerce doctrine.

CONCLUSION

The C.A.B.'s failure to apply the essential character/flow of commerce doctrine in this case was an unwarranted departure from longstanding federal court precedent and the agency's own practice of applying the essential character/flow of commerce doctrine to distinguish between movements in foreign and domestic air transportation. Moreover, the agency failed to provide a reasonable analysis supporting its abandonment of prior practice as required by this Court. Accordingly, Petitioners request grant of the foregoing petition for a writ of certiorari.

Respectfully submitted,

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Dated: December 18, 1986

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are not 'generally and independently available for purchase by domestic passengers without reference to prior or subsequent travel on international sectors.' " (Appendix B, page 53a.)

No. 86-998

IN THE

Supreme Court of the United States

October Term, 1986

JAPAN AIR LINES COMPANY, LTD.
and
SWISSAIR, SWISS AIR TRANSPORT
COMPANY, LTD.,
Petitioners,

v.

ELIZABETH HANFORD DOLE,
Secretary of Transportation,
Respondent.

APPENDIX TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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CASILLAS PRESS INC. – 1717 K STREET NW WASHINGTON DC 20037 – 223-1223

16 pp

TABLE OF CONTENTS

Page

APPENDIX A 1a
Decision of the United States Court of Appeals for the District of Columbia Circuit in *Japan Air Lines Co. v. Dole*, 801 F.2d 483 (1986).

APPENDIX B 23a
Opinion and Order on Discretionary Review of the Civil Aeronautics Board, in the *Visit USA Fare/ Export Inland Contract Rate Investigation*, Docket No. 40269, Order 84-8-55, August 10, 1984.

APPENDIX C 93a
Initial Decision of Administrative Law Judge John M. Vittone in the *Visit USA Fare/Export Inland Contract Rate Investigation*, Docket No. 40269, June 3, 1983.

APPENDIX D 155a
Federal Aviation Act, as Amended,
Section 101(24), 49 U.S.C. §1301(24)
Section 403(a), 49 U.S.C. §1373(a)
Section 1006, 49 U.S.C. §1486
Section 1102, 49 U.S.C. §1502

APPENDIX E 161a
Article 13 of the United States-Japan Air Transport Service Agreement of 1952.

APPENDIX F 163a
Section VII of the Annex to the United States-Switzerland Air Transport Services Interim Agreement of 1945, May 13, 1949.

APPENDIX A

801 F.2d 483

JAPAN AIR LINES COMPANY, LTD., Lufthansa German Airlines, and Swissair, Swiss Air Transport Company, Ltd., Petitioners,

v.

Elizabeth Hanford DOLE, Secretary of Transportation, Respondent.

Pan American World Airways, Inc., Trans World Airlines, Inc., Northwest Airlines, Inc., British Airways, Plc., Intervenors.

No. 84-1502.

United States Court of Appeals,
District of Columbia Circuit.

Argued Dec. 13, 1985.

Decided Sept. 19, 1986.

Proceeding was instituted on petition by foreign air carrier as to review of an order of the Civil Aeronautics Board. The Court of Appeals, McGowan, Senior Circuit Judge, held that adoption by the Board of a "carrier-restricted" test for purposes of differentiating foreign travel from domestic travel and determining whether fares and rates were discriminatory was not so inconsistent with prior "flow of commerce" test as to require more explanation than that provided.

Affirmed.

1. Aviation 102

Provision of Federal Aviation Act defining foreign air transportation as the carriage by aircraft by [sic] persons or property as a common carrier for compensation or hire or the carriage of mail by aircraft in commerce between a place in the United States and anyplace outside the United States does not require that foreign air transportation be defined by a "flow of commerce" test and permits the adoption of a "carrier-restricted" test to differentiate between foreign and domestic travel. Federal Aviation Act of 1958, § 101(24), as amended, 49 U.S.C.A. § 1301(24).

2. Aviation 102

Adoption by the Civil Aeronautics Board of a "carrier-restricted" test for purposes of differentiating foreign travel from domestic travel and determining whether fares and rates were discriminatory was not so inconsistent with prior "flow of commerce" test as to require more explanation than that provided. Federal Aviation Act of 1958, § 101(24), as amended, 49 U.S.C.A. § 1301(24).

3. Aviation 102

Bilateral agreements guaranteeing to carriers of signatory parties a "fair and equal opportunity to compete" in providing their services does not mean that a foreign carrier must be able to match fares and rates with its domestic competitors under all circumstances, but only means that a foreign carrier must be permitted to construct a matching fare on an interline basis. Federal Aviation Act of 1958, § 101(24), as amended, 49 U.S.C.A § 1301(24).

4. Aviation 102

A fair and equal opportunity to compete still exists if a foreign carrier, though absorbing some loss of its portion

of interline arrangement, can nevertheless construct a matching fare with domestic competitors. Federal Aviation Act of 1958, § 101(24), as amended, 49 U.S.C.A § 1301(24).

5. Aviation 102

Finding of Civil Aeronautics Board that bilateral agreement guaranteeing a fair and equal opportunity to compete to carriers of signatory parties was complied with as long as foreign carriers could find reasonably competitive alternative to domestic carriers' fares and rates was not clearly erroneous. Federal Aviation Act of 1958, § 101(24), as amended, 49 U.S.C.A § 1301(24).

6. Aviation 102

Standard adopted by the Civil Aeronautics Board for determining whether a rate amounted to unreasonable discrimination was meant to apply to foreign as well as to domestic air transportation. 5 U.S.C.A. § 706(2)(E); Federal Aviation Act of 1958, § 404(b), as amended, 49 U.S.C.A § 1374(b).

Petition for Review of an Order of the Civil Aeronautics Board.

Laurence A. Short, with whom David E. Short and Marc A. Bernstein, Washington, D.C., were on brief, for petitioners.

Barry L. Molar, Dept. of Transp., with whom J. Paul McGrath, Asst. Atty. Gen., Dept. of Justice, Kenneth N. Weinstein, Deputy Asst. General Counsel for Litigation, Dept. of Transp., Catherine G. O'Sullivan and Margaret G. Halpern, Dept. of Justice, Washington, D.C., were on brief, for respondent.

Michael J. Roberts, entered an appearance for intervenor, Pan American World Airways, Inc.

William C. Clarke, and James D. Tussing, New York City, entered an appearance for intervenor, British Airways, Plc.

Edmund E. Harvey, Washington, D.C., entered an appearance for intervenor, Trans World Airlines, Inc.

Ronald D. Eastman and Barry S. Spector, Washington, D.C. entered appearances for intervenor, Northwest Airlines, Inc.

Before ROBINSON and STARR, Circuit Judges, and McGOWAN, Senior Circuit Judge.

Opinion for the Court filed by Senior Circuit Judge McGOWAN.

McGOWAN, Senior Circuit Judge:

Petitioners, several foreign air carriers, challenge a Civil Aeronautics Board ("CAB" or "Board") order[1] governing

[1]The Civil Aeronautics Board ceased to exist on January 1, 1985. Orders such as the one at issue in this case remain in effect, however, and are administered by the Secretary of Transportation. Suits involving such orders continue, with the Secretary substituted as the respondent party. *See* Civil Aeronautics Board Sunset Act of 1984, Pub. L. No. 98-443, § 12(e), 98 Stat. 1703, 1711 (1984).

certain fares and a particular rate implemented by competing carriers with the Board's approval. We cannot say that the Board has departed from its statutory mandate in this matter. We therefore affirm the Board's order.

I. Background

On October 27, 1980, petitioners, Japan Air Lines Company, Ltd. ("JAL"), Lufthansa German Airlines ("Lufthansa") and Swissair, Swiss Air Transport Company, Ltd. ("Swissair"), joined by two companies not party to this petition for review, filed a complaint against the marketing of "Visit U.S.A." or "VUSA" fares by several domestic air carriers. VUSA fares generally permit a passenger visiting the United States from a foreign country to travel to various points within this country at a discount. The particular VUSA fares challenged in this litigation are "restricted," which means that they are available only to passengers who travel to and from the United States on the carrier offering the VUSA fare. Other VUSA fares are "unrestricted"; a passenger may choose one carrier for the trip from the foreign country to the United States and another carrier for travel within the United States.

On May 4, 1981, JAL filed an additional complaint against Northwest Airlines, Inc. ("Northwest") challenging Northwest's "Export Inland Contract Rate" ("ExIn rate"). The ExIn rate applied to freight carriage between Chicago-O'Hare and Seattle. The ExIn rate provided a discount for the Chicago-Seattle leg so long as the shipments were ultimately destined for Hong Kong, Japan, South Korea, the Philippines, or Taiwan. Shipment from Seattle to the Far East could be on any United States or foreign air carrier, or by ocean vessel, at any international tariff rate.

Petitioners challenged the VUSA fares and ExIn rate on the theory that they involved foreign air transportation, and thus that the carriers were required to file them in their international tariffs. In addition, the complaints alleged that the fares and rate were contrary to the provisions of the applicable Civil Air Transport Agreements, which guarantee foreign carriers a fair and equal opportunity to compete. Finally, the complaints alleged that the fares and rate were unjustly discriminatory, as that term is used in the Federal Aviation Act of 1958.

The complaints were consolidated. Various domestic air carriers intervened in the proceedings. In September, 1982, an Administrative Law Judge ("ALJ") conducted a hearing on the complaints. The ALJ issued his initial decision on June 3, 1983. The ALJ found that the fares and rate involved foreign air transportation (thus requiring filing in international tariffs). The ALJ also held, however, that the fares and rate did not deny the foreign carriers a fair and equal opportunity to compete and were not unjustly discriminatory. Joint Appendix ("J.A.") at 169-231 (initial decision).

Both foreign and domestic carriers petitioned the CAB to take discretionary review of the initial decision. The Board granted those petitions and, on August 10, 1984, issued its decision. The Board upheld the ALJ's finding that the VUSA fares involved foreign air transportation, but found that the ExIn rate concerned domestic carriage. The Board also affirmed the ALJ's finding that the fares and rate did not deny the foreign carriers a fair and equal opportunity to compete, and the finding that the fares and rate were not unjustly discriminatory. J.A. at 2-49 (CAB decision).

In their petition for review to this court, petitioners did

not challenge the Board's finding that the VUSA fares involved foreign air transportation. Br. of Petitioners at 3-4. Petitioners launch an omnibus challenge to the remainder of the Board decision. We treat their objections in the sequence followed in the Board decision.

II. Analysis

A. *ExIn Rate as International Rate*

The CAB held that the ExIn rate did not involve foreign air transportation because it was not restricted to combination with any particular carrier on the foreign portion of any shipment. J.A. at 30. The Board reasoned that if such a rate were available on equal terms, it would be economically independent of the international travel to which it is tied for marketing purposes:

> A carrier simply will not price such a fare below its cost, because it has no interest in subsidizing the services of other carriers. Without the ability to restrict participation in the international travel to particular carriers, the offering carrier will have no leverage to require that profits from the international travel subsidize its domestic service. And without a carrier restriction, its fares *prima facie* will be competitively evenhanded in international service.

Id.

Petitioners object to the application of this test on the ground that it is inconsistent with the "flow of commerce" test for differentiating foreign travel from domestic. Under the "flow of commerce" test, according to petitioners, the distinction must be drawn by considering the "essential character of the movement." This, in turn, is determined largely by reference to the intent of the passenger or ship-

per, *ie.*, whether he intended at the outset to engage in a through journey. *See* Br. of petitioners at 9. The rate at issue in this case, according to petitioners involves foreign air transporation because the intent of any shipper who uses the rate is to transport from Chicago ultimately to a foreign destination. Petitioners' essential complaint is that the CAB has previously applied the "flow of commerce" test in these circumstances and that the rejection of that test and the adoption of the "carrier-restriction" test is unaccompanied by an adequate explanation.

It is by now a familiar rule that a court owes some deference to an agency's interpretation of its organic statutes. "[I]f the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute." *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 (1984). Despite this requirement of deference, we cannot countenance arbitrariness. Indeed, there exists a presumption against unexplained changes in agency interpretations. *See Motor Vehicle Mfrs. Assoc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 41-42, 103 S.Ct. 2856, 2865, 2866, 77 L.Ed.2d 443 (1983). In particular, we have cautioned that "an agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored, and if an agency glosses over or swerves from prior precedents without discussion it may cross the line from tolerably terse to intolerably mute." *Airmark Corp. v. FAA*, 758 F.2d 685, 692 (D.C.Cir.1985) (quoting *Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C.Cir.1970), *cert. denied*, 403 U.S. 923, 91 S.Ct. 2229, 29 L.Ed.2d 125 (1971)). We hold that the CAB adoption of the "carrier-restricted" test in this case was not a significant change

from prior interpretations. We cannot say, therefore, that the agency has violated its obligation to interpret consistently the statutes under which it operates.

Our analysis of the issue begins with a review of the statute. The Federal Aviation Act of 1958 explicitly distinguishes between "interstate air transportation," "overseas air transportation," and "foreign air transportation." In particular, " 'foreign air transportation' . . . mean[s] the carriage by aircraft of persons or property as a common carrier for compensation or hire or the carriage of mail by aircraft, in commerce between . . . (c) a place in the United States and any place outside thereof[.]" 49 U.S.C. § 1301(24) (1982).

[1] On its face, the statute does not require that "foreign air transportation" be defined by a "flow of commerce" test. Petitioners insist, however, that CAB interpretation of the term has embodied this test. We must reject that argument. It is apparent that the CAB has never stated that the "flow of commerce" test is the *sole* test for determining whether air transportation is foreign. We have carefuly reviewed the CAB cases cited by petitioners and find that they do not support such an absolute view.[2]

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[2]We may briefly summarize our reading of each of these CAB cases, proceeding in chronological order. In *Canadian Colonial Airways, Inc. – Investigation*, 2 CAB 752 (1941), the Board determined that flights between Montreal, Canada and Nassau, Bahamas with an overnight stop in Jacksonville, Florida retained their foreign character despite the stop in the United States. The Board remarked that the stop was "merely an incidental part of the whole trip to the ultimate destination." *Id.* at 754. The Board cited Supreme Court cases which refer to the "flow of commerce" test, *see id.*, but did not state that this was the only applicable test.

In *Resort Airlines Miami Stopover Investigation*, 19 CAB 1 (1954), the Board held that, for tours from United States cities to Caribbean

In addition, as the Board noted in this case, "the Board has never given unqualified acceptance to an origin-desti-

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resort areas, a stopover in Miami, Florida of not more than one-third the duration of the tour would mean that the entire trip was foreign. The Board noted that the question was whether the stopover was "the principal or dominant part of the tour." *Id.* at 8. Again, the Board referred to Supreme Court precedent involving the "flow of commerce" test, but did not state that that test was the sole basis for defining foreign air transportation. *See id.* at n. 14.

In *Foreign Off-Route Charter Service Investigation,* 27 CAB 196 (1958), the Board simply adhered to a prior policy of permitting foreign air carriers, which had been granted permits along designated routes, to schedule additional flights from a United States point named in the permit to points beyond, provided that the flights operated via the described United States terminal point. The Board gave as reasons for this policy "comity and administrative simplicity," and did not even refer to the "flow of commerce" test. *Id.* at 200.

In *Eastern Airlines, Inc., Enforcement Proceeding,* 40 CAB 745 (1964), an airline had given discount fares to travel agents for trips from points in the United States to Miami, Florida, only if the agents' trips extended beyond Miami to some foreign or overseas point. Such discounts were authorized by law only if the trips were considered overseas or foreign travel. The Board decided to terminate its enforcement proceeding in this matter. In so doing, the Board stated that "[a]s a general rule, the destination which was intended by the passenger when he begins the journey and which was known to the carrier and for which he purchased a ticket determines the character of the trip." *Id.* at 747. Despite this general rule, however, the Board chose an alternate procedure for resolving the case, dismissing the proceeding and instituting a proceeding to establish international agreement for limitations on stopovers. *Id.* at 748.

In *Airfreight Forwarders, Revocations,* 65 CAB 1605 (1974), the CAB sought to revoke certain unused domestic operating authorizations. One carrier contended that it was using its domestic authorization because its international carriage also included a domestic leg. The Board rejected this argument, noting, in part, that "whether a shipment is moving in domestic or international air transportation is determined by its ultimate destination. . . ." *Id.* at 1608. This statement, in context, does not establish that destination is the sole test for distinguishing domestic from international air transportation. The

nation test, and its limited consideration of passenger intent in other statutory contexts was to aid in determining whether there was a 'significant break' in the journey. Where another test, such as a carrier's geographic operations, was more relevant to the statutory provision and policies at issue, flow of commerce principles were readily rejected." J.A. at 25.

Recent support for that proposition appears in the Board's *Tariff Flexibility Rulemaking,* 46 Fed. Reg. 46,787 (1981). That rulemaking was conducted as part of the Board's effort to provide an orderly transition into the pro-competitive scheme mandated by Congress in the Airline Deregulation Act of 1978, Pub.L. No. 95-504, 92 Stat. 1705 (1978). The Board sought to establish a flexibile tariff-filing procedure for domestic passenger fares. Some

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Board relied, in *Airfreight Forwarders,* on the decision in *Canadian Colonial Airways, Inc. – Investigation,* 2 CAB 752 (1941), a case which we have already noted does not stand for that general proposition. Indeed, the issue in *Airfreight Forwarders* was really only whether a shipment moving on a waybill between a point in the United States and a point outside would be international regardless of whether a change of planes was made at the gateway. *Airfreight Forwarders,* 65 CAB at 1608. The Board simply decided that question in the affirmative.

Finally, in *Air Tungaru-UTA, Wet-Lease Exemption,* 90 CAB 606 (1981), Air Tungaru, the flag carrier of the Republic of Kiribati, requested a disclaimer of jurisdiction over the Christmas Island to Tahiti portion of a route from Honolulu to Tahiti via Christmas Island. Air Tungaru proposed to provide service from Honolulu to Christmas Island, but to lease its aircraft to Union de Transport Ariens for the Christmas Island-Tahiti operation. Since Christmas Island and Tahiti are not United States possessions, that route alone would not be in foreign air transportation for purposes of the Act. The Board concluded, however, that the two carriers intended to offer joint services over the Christmas Island-Tahiti segment and, thus, that the entire route was in foreign air transportation. *Id.* at 608. The Board, again, did not even mention the "flow of commerce" test in-deciding the case.

parties objected, however, that the provision in most bilateral treaties giving foreign governments a right to have advance notice of prices for foreign air transportation requires the filing of binding domestic tariffs. In response, the Board stated that the test for foreign air transportation is not restricted to the ultimate origin and destination of the passenger or shipper. *See* 46 Fed. Reg. at 46,791-92. The Board explained that, if adopted, such a test "would require the filing of an exact fare for every domestic market because service in any domestic market might be combined with service to a foreign point." *Id.* at 46,791.

[2] The *Tariff Flexibility Rulemaking* establishes the proposition that "slavish adherence" to the intent of the passenger is not the rule. *See* Reply Br. of Petitioners at 13. As the Board clearly stated in that proceeding, "we have rejected that test when necessary to preserve a fundamental policy of the Act." 46 Fed. Reg. at 46,792. We find the Board's adoption, in this case, of a "carrier-restricted" test for distinguishing foreign from domestic air transportation not so inconsistent with prior precedent as to require more explanation than that provided by the Board.[3]

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[3]Petitioners also suggest that the "carrier-restricted" test is defective because the record in this case does not suppport the considerations underlying the test. Br. of Petitioners at 32. We have reviewed the alleged defects in the record and must reject this attack on the foundation of the "carrier-restricted" test.

We mention one brief example of petitioners' objections on this score. Petitioners object to a passage in the Board's decision which rejects the ALJ's initial decision because the ALJ's approach would require the filing of fares and rates in other cases which would not ordinarily require such filing. *See* Br. of Petitioners at 33 (referring to Board decision, J.A. at 21-22). Petitioners suggest that it was improper for the Board to refer to matters extrinsic to the record in this case. *Id.* at 34. We find nothing impermissible in this practice. Peti-

B. *Equal Opportunity to Compete*

The ALJ determined that the VUSA fares and the Ex-In rate were consistent with the provisions of various bilateral agreements with foreign nations that guarantee to the carriers of the signatory parties a "fair and equal opportunity to compete" in providing services.[4] Only JAL and Lufthansa challenged that conclusion. *See* J.A. at 35-36 & n. 51. The Board affirmed the ALJ's findings and conclusions. *See* J.A. at 35. JAL and Lufthansa press their objections in this court.

Again, the substance of petitioners' claim is that the Board has acted inconsistently. The Board has always insisted, according to petitioners, that carriers must be able to match fares and rates offered by their competitors. In this case, however, the Board held:

> A "fair and equal" opportunity does not mean an identical opportunity, nor does it exempt carriers from normal commercial practices and the consequences of open price competition. In essence, what is required is that foreign carriers have the opportunity to offer reasonably com-

tioners mistake the prohibition against reference to factual matters outside the record for a more general prohibition that would preclude an agency from considering how a rule adopted in one case might affect other cases. No such general prohibition exists. Indeed, it is the essence of the adjudicatory process to reason from one case to another, including consideration of hypothetical applications of a rule to other circumstances. It is well-settled, moreover, that an agency retains substantial discretion to develop new rules through adjudicatory proceedings. *SEC v. Chenery Corp.*, 332 U.S. 194, 203, 67 S.Ct. 1575, 1580, 1581, 91 L.Ed. 1995 (1947).

[4]*See, e.g.*, United States-Federal Republic of Germany Air Transport Services Agreement of 1955, Art. 8, 7 U.S.T. 527, 532, T.I.A.S. No. 3536; United States-Japan Air Transport Services Agreement of 1952, Art. 10, 4 U.S.T. 1948, 1953, T.I.A.S. No. 2854.

> petitive alternatives to particular internal point fares. The issue is therefore primarily a factual one, and there is no simple formula for determining a violation of these bilateral provisions.

J.A. at 37. Petitioners insist that the "reasonably competitive alternatives" approach adopted in this case is inconsistent with the requirement of exact fare-matching expressed in prior cases. We find no such inconsistency.

Our review of this question is informed by the acknowledged need to defer to the expertise of the Board — the agency responsible in part for negotiating the very executive agreements whose interpretation is now in dispute. *See Sumitomo Shoji America, Inc. v. Avagliano,* 457 U.S. 176, 184-85, 102 S.Ct. 2374, 2379-2380, 72 L.Ed. 2d 765 (1982); *Collins v. Weinberger,* 707 F.2d 1518, 1522 (D.C.Cir.1983). We note, in addition, that despite the protestations of petitioners in this case, the governments of these foreign carriers' home countries have lodged no objection to the Board's interpretation of these agreements.

[3, 4] Petitioners cite several cases for the proposition that the requirement of a "fair and equal opportunity to compete" means that a foreign carrier must be able to match fares and rates with its domestic competitors under all circumstances. *See, e.g., Air India, Discriminatory Fares,* 92 CAB 753 (1981); *TWA, re German Discriminatory Practices,* 88 CAB 952 (1981). These cases, however, merely establish that a carrier must be permitted to construct a matching fare on an interline basis. Where a carrier can construct a matching fare but must absorb some loss on its portion of the interline arrangement, the Board has held that a fair and equal opportunity to compete still exists. *See, e.g., Continental Air Lines, Emergency Ex-*

emption, 102 CAB 755, 758-59 (1983); *Continental Excursion Fares, Qantas Complaint,* 96 CAB 792, 794-95 (1982). The Board's use of the term "reasonably competitive alternatives" in this case does not constitute the adoption of some new test. Rather, it merely describes application of the traditional rule to interline arrangements.

[5] Petitioners also attack as erroneous the Board's factual conclusion that the foreign carriers can find reasonably competitive alternatives to the domestic carriers' fares and rate. Br. of Petitioners at 57-60. The substance of their argument is that foreign carriers cannot, under the laws of their home countries, "prorate" to provide matching fares and rates.[5] This court may set aside the Board's finding on this score only if it is "unsupported by substantial evidence[.]" 5 U.S.C. § 706(2)(E) (1982). "Substantial evidence" need not be overwhelming evidence. "A factual finding is supported by substantial evidence if the record contains 'such relevant evidence as a reasonable mind might accept as adequate to support a conclusion.' " *American Fin. Services Assoc. v. FTC,* 767 F.2d 957, 985 (D.C.Cir.1985) (quoting *American Textile Mfrs. Inst., Inc. v. Donovan,* 452 U.S. 490, 522, 101 S.Ct. 2478, 2497, 69 L.Ed.2d 185 (1981)). On our review of this record, we find the Board's findings adequately supported, not only

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[5]In particular, petitioners note that the restricted VUSA fares offered by the domestic carriers are $76 to $250 less costly than the unrestricted VUSA fares. Br. of Petitioners at 51. The Board's answer to this problem, in part, was that the foreign carriers could make "prorate" arrangements. Under such agreements, the foreign carrier would pay the domestic carrier the difference between its ordinary fare or rate and the lower fare or rate that the foreign carrier proposed to charge the passenger or shipper for the domestic leg of the trip. *See* J.A. at 41-43.

as to the availability of prorate arrangements,[6] but also as to the general ability of the foreign carriers to compete with the domestic carriers.[7]

C. *Unjust Discrimination*

[6] The Federal Aviation Act of 1958 forbids "unjust discrimination" against any particular person, port, locality, or description of traffic in air transportation. *See* 49 U.S.C. § 1374(b) (1982). To test whether that prohibition forbids the fares and rate at issue in this case, the CAB applied the standards of PS-93, 14 C.F.R. § 399.36 (1985).[8] The Board found, and petitioners now concede, that the fares and rate were lawful under those standards. Peti-

[6]The ALJ found, and the Board agreed, for example, that prorate arrangements are a standard practice in the industry. *See* J.A. at 221 (initial decision); *id.* at 43 (Board order). We find this factual conclusion well supported.

[7]The ALJ concluded, for example, that, through the use of unrestricted VUSA fares, Lufthansa had been able to carry more VUSA passengers in the United States-Germany market than any United States carrier. J.A. at 218 (initial decision). Petitioners nowhere challenge this fundamental fact.

[8]PS-93, 14 C.F.R. § 399 (1985) provides, in pertinent part:

> (b) Except in unusual circumstances . . . the Board will find a rate for domestic air transportation to constitute unreasonable discrimination only if:
>
> (1) There is a reasonable probability that the rate will result in significant long-run economic injury to passengers or shippers;
>
> (2) The rate is in fact discriminatory according to a reasonable cost allocation or other rational basis;
>
> (3) The rate does not provide transportation or other statutorily recognized benefits that justify the discrimination; and
>
> (4) Actual and potential competitive forces cannot reliably be expected to eliminate the undesirable effects of the discrimination within a reasonable period.

tioners insist, however, that the PS-93 standards were intended to apply only to domestic fares and rates. Moreover, they argue, application of these standards to the fares and rate at issue in this case is inconsistent with prior precedent, which would otherwise compel a finding that the fares and rate are unjustly discriminatory. In sum, in their view, the Board's use of the PS-93 standards in this case was arbitrary and capricious. We cannot agree.

We reemphasize that an agency is not forbidden from changing policy when such changes are supported by adequate reasons. *See Airmark Corp.*, 758 F.2d at 692. In addition, we note, an agency enjoys substantial discretion to proceed with such changes either by rule or by adjudication. *See SEC v. Chenery Corp.*, 332 U.S. 194, 203, 67 S.Ct. 1575, 1580, 1581, 91 L.Ed. 1995 (1947); *British Caledonian Airways, Ltd. v. CAB*, 584 F.2d 982, 984 (D.C.Cir. 1978). The Board acted in this case in an adjudicative proceeding. Even if the extension of PS-93 to foreign air transportation may be said to establish a novel rule, inconsistent with prior precedent, we may not upset such changes unless we are convinced that the agency has changed course without carefully considering the reasons for, and consequences of, such a change. We consider this question in light of petitioners' remaining objections.

First, petitioners argue that the Board's order in this case violates the plain wording of PS-93, which restricts itself to domestic and overseas air transportation. Br. of Petitioners at 64. The Board's PS-93 policy statement was developed in response to the reduction of the Board's domestic rate authority by the Airline Deregulation Act of 1978, Pub.L. No. 95-504, 92 Stat. 1705 (1978). Despite this initial impetus, however, the Board recognized, in adopting the policy statement, that it might apply to for-

eign air transportation as well.[9] Since then, the Board has applied PS-93 to foreign air transportation on a case-by-case basis. *See, e.g., Lufthansa v. Pan Am Fares Complaint*, 93 CAB 799, 802 (1982); Charter Trips and Special Services; Removal of Limitations on Off-Route and Cargo Charters, 45 Fed.Reg. 53,358 (Aug. 11, 1980). We find these circumstances readily distinguishable from cases in which an agency has adopted a policy statement for use in

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[9]The Board addressed this potential application in its statement adopting PS-93:

> While it is true that the original impetus for this policy statement was the ADA of 1978 with its implicit emphasis upon domestic aviation, the Board did not intent [sic] to preclude a common international pricing application. We invited comments but made no specific proposals on the international pricing aspects of this subject, and therefore received few concrete proposals or arguments on it. Consequently, we will limit this policy statement to domestic and overseas air transportation.
>
> Nevertheless, the passage of the International Air Transportation Competition Act of 1978, after our initial policy proposal here, has substantially altered the statutory and policy framework within which we consider international pricing and entry issues. In many pertinent respects, the framework is now similar -- if not identical -- to the domestic area. While there are *ad hoc* circumstantial differences, such as limited entry in some international markets and detailed pricing control by a number of foreign governments, we believe that many of the fundamental policy considerations that lead us to issue this statement are equally applicable to foreign air transportation. Our staff is now considering this issue, and it also has been raised by the commentors in EDR-351B and EDR-383, by which we proposed, among other things, to permit cargo charters on scheduled flights. Thus, we will address this question in more detail shortly.

45 Fed.Reg. 36,062 (May 29, 1980).

one area and then expanded its application, without explanation, to another area.[10]

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[10]Petitioners' principal authority for the proposition that an agency may not expand a policy statement beyond the area of its intitial focus is *Advanced Micro Devices v. CAB*, 742 F.2d 1520 (D.C.Cir. 1984). We find that precedent inapposite. In *Advanced Micro*, the CAB had initially proposed to allow carriers to increase international cargo rates up to five percent above a standard foreign rate level and to decrease them without limit. The Board not only would not suspend any rate in the zone, but would, without further investigation, conclusively presume the rate to be economically justified. *Id*. at 1524. The final rule, however, limited the use of the zone to suspension decisions. *Id*. at 1526. Despite this express limitation to suspension decisions, the Board, in *Advanced Micro*, approved an agreement to change rates on the basis of policy alone, without further investigation. *Id*. at 1527. This court disallowed the expansion of the policy statement, noting both that the policy was not created to determine the reasonableness of final rates and that the Board had, in following the policy statement, failed to make certain required findings. *Id*. at 1540.

The *Advanced Micro* situation diverges from that of the instant case in several important respects. First, in *Advanced Micro*, the Board expressly stated that it would not expand the policy statement beyond the suspension decisions it was designed to cover. By contrast, here, the Board noted that many of the fundamental policy cosiderations underlying PS-93 would also apply to foreign air transportation. 45 Fed.Reg. 36,062 (May 29, 1980). The Board also stated that it intended to consider the application of PS-93 to foreign air transportation in the context of individual cases. *Id*.

Second, in *Advanced Micro*, we expressed concern that the Board had failed to provide a "carefully reasoned and factually supported explanation for any departure from past practice." *Advanced Micro*, 742 F.2d at 1545. In the instant case, the Board provided a full statement of its reasons for applying PS-93 to foreign air transportation. *See* J.A. at 58 (order instituting investigation) (requesting factual information on applicability of PS-93); *id*. at 200-202 (initial decision of ALJ) (explaining applicability of PS-93); *id*. at 45 (CAB opinion and order on discretionary review) (explaining applicability of PS-93).

Finally, in *Advanced Micro*, the Board applied its policy statement wholesale, without making the findings required under the statute. *Advanced Micro*, 742 F.2d at 1540. We find no such wholesale adoption of the policy statement here. Instead, the Board applied the prin-

Second, petitioners argue that the application of the PS-93 criteria to complaints of discrimination in foreign air transportation is improper because it rests on the premise that foreign air transportation has been deregulated to the same extent as domestic air transportation. *See* Br. of Petitioners at 68. Foreign air transportation has not been deregulated, they argue, because Congress has not changed the unjust discrimination prohibition of 49 U.S.C. § 1374(b) (1982). We reject this view. Congress, in the International Air Transportation Competition Act, expressly directed the CAB to regulate with a pro-competitive outlook.[11] While the initial impetus for PS-93 was the Airline Deregulation Act of 1978, the Board could properly extend the application of PS-93 to foreign air transportation in light of the clear congressional directive in the International Air Transportation Competition Act.

Finally, petitioners argue that the Board's use of PS-93 is an unexplained departure from prior precedent. Br. of Petitioners at 69. This departure, they insist, is all the more egregious because Congress, in enacting the Airline Deregulation Act of 1978, expressed its approval of the

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ciples of the policy statement as only one source of legal authority. The Board also considered pre-deregulation case law, and explained how the case fit into that framework, as affected by PS-93. *See* J.A. at 45-49.

[11]Congress provided, in particular:

> In the exercise and performance of its powers and duties under this chapter, the Board shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity:
>
> * * * * *
>
> (4) the placement of maximum reliance on competitive market forces and on actual and potential competition. . . .

49 U.S.C. § 1302(a) (1982).

Board's prior decisions concerning unlawful discrimination. Br. of Petitioners at 69-70. We reject the view that Congress, in the Airline Deregulation Act, froze Board precedent on unlawful discrimination. The sole basis for petitioners' assertion is a brief comment in a committee report on the Airline Deregulation Act: "The committee believes that current Board case law defining unlawfully discriminatory, preferential, and prejudicial carrier prices and practices are [sic] generally satisfactory." S.Rep. No. 631, 95th Cong., 2d Sess. 109 (1978). This statement must be read in the context of the overall deregulatory scheme implemented by Congress. Congress initially removed the Board's power to set rates after the Board made a finding of unlawful discrimination in domestic or overseas air transportation. The Board was empowered to remove the discrimination only. *See* Airline Deregulation Act of 1978, Pub.L. No. 95-504, § 37, 92 Stat. 1705, 1741-43 (1978). Eventually, Congress eliminated the Board's power over unlawful discrimination in domestic and overseas air transportation altogether. 49 U.S.C. § 1551(a)(2)(B) (1982). Thus, the offhand remark in the committee report appears to mean little more than that Congress viewed Board precedent on unlawful discrimination as tolerable during the initial phase of deregulation. Viewed in context, this remark can hardly be taken to mean that Congress intended this precedent to remain untouched forever.

Conclusion

The thrust of petitioners' claims in this case is that the CAB has acted inconsistently in a number of areas. We emphasize that it remains our province to review agency treatment of similar cases to prevent arbitrary and capricious action. The need for such review follows from a de-

sire for fair play and fidelity to congressional objectives. Our inquiry into agency action, however, must be tempered by the recognition that the circumstances surrounding agency regulation do not remain static. In particular, by altering the statutory framework within which an agency operates, Congess may dramatically shift the direction of an agency's regulation. In such circumstances, an agency may, with appropriate explanation, alter its prior policies without fear of judicial interference. Finding no error in the Board's order in this case, we affirm.

It is so ordered.

APPENDIX B

Order 84-8-55

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D.C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D.C.
on the 10th day of August, 1984

VISIT USA FARE/EXPORT INLAND CONTRACT RATE INVESTIGATION	Docket 40269

ERRATUM

1. The word "is" should be inserted before the word "unsubstantiated" in line 24 on page 24.

2. Lines 4, 5 and 6 of footnote 41, on page 27, should be changed to read:

> (residents) and are not available to any purely domestic traffic; and (3) the overwhelming majority of VUSA tickets and itineraries are purchased and prepared at foreign origin.

Dated September 12, 1984

Order 84-8-55

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D.C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D.C.
on the 10th day of August, 1984

VISIT USA FARE/EXPORT INLAND CONTRACT RATE INVESTIGATION	:	Docket 40269

OPINION AND ORDER ON DISCRETIONARY REVIEW

I. The Proceedings

The Board instituted this proceeding to investigate the lawfulness of certain "Visit USA" (VUSA) fares of Northwest Airlines, Inc. (Northwest), Pan Am World Airways, Inc. (Pan Am), and Trans World Airlines, Inc. (TWA) and of an "Export Inland" Contract (Contract) rate offered by Northwest.[1] Its genesis was a complaint by Japan Air Lines Company, Ltd. (JAL) and Lufthansa German Airlines (Lufthansa) seeking the suspension and investigation

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[1]Order 81-11-182, December 1, 1981.

of these VUSA fares,[2] and a complaint by JAL against the Contract rate of Northwest. Capitol Air's VUSA fare was consolidated after a complaint was filed by Lufthansa.[3] British Airways was granted leave to intervene as a result of its complaints (Dockets 40861 and 40945) against revisions by TWA and Pan Am to the VUSA fares under investigation in certain United States-United Kingdom markets.

The complaints challenged the lawfulness of those VUSA fares which, by their term, were available only in conjunction with the purchase and use of a round-trip international ticket on the issuing VUSA carrier or on a restricted number of listed participating carriers. The complainants contended that this carrier restriction (1) made the VUSA fares international for tariff filing and review purposes under the Federal Aviation Act of 1958, as amended (the Act), and the bilateral air transport agreements between the U.S. and their governments, (2) denied them their bilateral rights to a fair opportunity to compete for VUSA traffic, (3) violated the U.S. antitrust laws, and (4) was unjustly discriminatory under sections 404(b) and 1002 of the Act against non-VUSA traffic in general and their traffic in particular.

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[2]Dockets 38899 and 39595. Philippine Airlines, Inc., Singapore Airlines, Limited, and Swissair, Swiss Air Transport Company, Ltd., joined in the complaint in Docket 38899. China Airlines, Ltd., filed a separate complaint in Docket 39028. These carriers have withdrawn from the investigation. (*See* Orders of the Administrative Law Judge, February 19, June 23, and August 2, 1982). The complaint in Docket 38899 also named the VUSA fares of Western Air Lines, Inc., and Braniff Airways, Inc. The complaint against Western was dismissed by Order 81-11-182 at the request of the complainants. Braniff was dismissed as a party after it ceased operations and entered into reorganization proceedings under the Bankruptcy Code. (*See* Order of the ALJ, May 28, 1982).

[3]Docket 40420. Order 82-2-30, February 5, 1982.

The Contract rate was challenged essentially because it was available only in conjunction with an onward international movement from the U.S. gateway to points in Asia, although without restriction as to carrier or even transportation mode. The complaint alleged that this restricted availability made the rate international for tariff filing and review purposes and rendered it unjustly discriminatory under sections 404(b) and 1002 of the Act.

Order 81-11-182 defined the primary issue in this proceeding as whether the VUSA fares and the Contract rate are unlawful under the Act or contrary to the provisions of the civil air transport agreements between the United States and the national governments of the complaining carriers. The order expressly included as subissues: (a) should the VUSA fares and/or the Contract rate be classified as domestic or international for filing and review purposes under the Act and the relevant bilaterals; (b) are the VUSA fares and/or the Contract rate unjustly discriminatory within the meaning of sections 404(b) and 1002; (c) are the VUSA fares and/or the Contract rate inconsistent with the provisions of the bilaterals which guarantee a fair opportunity to compete; and (d) do the VUSA fares violate section 1 of the Sherman Act.[4]

Following oral hearing procedures, Administrative Law Judge John M. Vittone served his Initial Decision on June 3, 1983. He concluded that the VUSA fares and the Contract rate at issue:

1. should be classified as international under the Act and the relevant bilaterals, and filed with, and reviewed by, the Board and affected foreign governments;

[4] JAL and Lufthansa moved on June 17, 1982, to amend their complaint to withdraw the allegation of a section 1 violation. By Order of the ALJ, dated July 8, 1982, this subissue was dismissed from the case.

2. are not unjustly discriminatory within the meaning of sections 404(b) and 1002 of the Act; and

3. are consistent with the bilateral provisions which guarantee a fair opportunity to compete.

Petitions for discretionary review were filed by most of the parties. Northwest, TWA, Pan Am, the Department of Transportation (DOT), and the Bureau of International Aviation (BIA) seek reversal of the ALJ's conclusion that the fares and rate at issue should be treated as international for filing and review purposes. JAL and Lufthansa seek reversal of the ALJ's conclusions regarding discrimination and bilateral rights to compete.

Answers to the petitions were filed by JAL and Lufthansa urging affirmance of the ALJ's decision on the tariff filing issue, by British Airways urging affirmance of the initial decision in its entirety, and by Capitol Air, Northwest, TWA, Pan Am and BIA urging affirmance of the ALJ's decision on the discrimination and bilateral right to compete issues.

By Order 83-7-101, the Board took review of the Initial Decision in its entirety. Briefs and reply briefs have been filed and the case stands submitted for decision.

II. Summary of Findings and Conclusions

Upon consideration, we find and conclude that: (1) the carrier-restricted VUSA fares at issue should be classified as international for filing and review purposes under the Act and the relevant bilaterals; (2) the export-restricted Contract rate is not international for filing and review purposes; (3) the fares and the rate at issue are not inconsistent with bilateral guarantees of a fair and equal opportunity to compete; and (4) the fares and the rate at issue

are not unjustly discriminatory under sections 404(b) and 1002 of the Act.[5]

Our major departure from the Initial Decision concerns the test for resolving the tariff-filing, or "definitional," issue. We agree with the ALJ's conclusion that the carrier-restricted VUSA fares at issue should henceforth be considered international for filing and review purposes,[6] but we would modify his test and rationale in important respects to more adequately distinguish "unrestricted" VUSA fares and make clear that the latter need not be filed. We will also reverse his conclusion that the export-restricted Contract rate is international for filing and review purposes, finding it essentially analogous to unrestricted domestic VUSA fares under our analysis.

As discussed below, this is a limited case. It concerns fares and rates between domestic points which are not merely "combinable" with foreign travel, *i.e.* available to both purely domestic and international passengers, but rather are available *only* in conjunction with international travel. This threshold distinction does raise certain definitional difficulties under traditional analyses. At the same time, the carrier restriction raises other, more substantive concerns. Within the limited context of this case, we conclude that the carrier restriction challenged by the complainants and accepted as at least one decisional factor by

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[5]Except to the extent modified here, we adopt the ALJ's findings and conclusions as our own. His Initial Decision is attached as an Appendix.

[6]More specifically, we conclude, as a matter of statutory interpretation, that the carrier-restricted VUSA fares at issue are in "foreign air transportation" for the limited purpose of applying section 403 of the Act as amended by section 1601(a)(2)(A), and we further conclude that this interpretation is consistent with, although not necessarily required by, the tariff-filing and review provisions of the bilaterals of record.

the ALJ is a realistic and administratively feasible line to draw for tariff filing and review purposes. We can justifiably require the filing of fares and rates available only in conjunction with separately ticketed international travel if, but only if, they are also carrier restricted as to the international travel. If they are equally available to the passengers of all carriers, they are essentially independent domestic fares in the economic and competitive sense, and domestic regulatory interests greatly outweigh foreign regulatory interests. The carrier restriction distinction is not wholly "novel," as BIA, DOT and the U.S. carriers assert, but more importantly, it accords with (1) economic reality, (2) competitive reality, and (3) a balancing of competing regulatory interests. It is a line which all governments can live with and all carriers can use.

We believe that our filing test is one of general applicability and will apply it in determining the filing status of similar fares and rates, whether offered abroad by U.S. carriers or in the U.S. by foreign carriers. Air carriers and foreign air carriers will be given 30 days from the date of service of this decision to file current fares with the Board and with foreign governments consistent with bilateral obligations. Once filed, the fares may be advertised "subject to governmental approval" to the extent permitted under normal statutory and bilateral procedures. We would expect tickets sold prior to the filing date to be honored according to their terms regardless of the date of transportation.[7]

[7]In our judgment, 30 days is a reasonable balance between the need to allow all carriers an opportunity to review current VUSA programs and revise them, if necessary, and the interest of foreign governments in reviewing carrier-restricted VUSA fares. Allowing carriers to offer current VUSA fares pending filing and governmental review will insure due process and prevent an uneconomic and unfair hiatus in marketing programs and passenger travel arrangements

III. VUSA Fares Generally and Those at Issue

A. Conditions and Restrictions

VUSA fares have been offered since 1968, when the Board first expressly approved discount fares for travel between U.S. points restricted for sale to foreign residents.[8] They take many forms, ranging from flat fares for selected point-to-point travel to flat fares for "unlimited" system-wide travel. Most certificated U.S. carriers now offer one or more such fares.[9] Capitol's point-to-point variety at issue in this proceeding, for example, originally permited round-trip on-line transportation between New York and either Chicago, Los Angeles, Miami or San Francisco for $189.52, and between New York and San Juan for $199. Alternatively, it permitted westbound-only travel from New York to either Los Angeles or San Francisco for $92.38 (CL-1R-4). Also common are the "unlimited" travel variety which, at the time of the hearing, ranged in price from approximately $400 to $600.[10] Subject to varying restrictions, these fares permit extensive optional travel and stopovers over the domestic route system of the U.S. carrier offering the fare for specified times ranging from 14 to 90 days. The Pan Am, TWA and Northwest fares at issue are of this variety. In some cases, Canada is

[8] *Discount USA Fares*, 48 CAB 892 (1968), available only to foreign residents and U.S. government personnel stationed outside the Western Hemisphere, were found not to be unjustly discriminatory because of their expected contribution to the U.S. balance of payments. The fares were filed domestic tariffs without challenge, and no definitional issue was raised.

[9] In addition to Pan Am, Northwest, TWA and Capitol, at least Air California, Alaska, Delta, Eastern, Republic, Ozark, Continental, USAir, Pacific Southwest, Western, Wien, World, United, American and Aloha offered VUSA fares in 1982. (PA-12; I.D. at 3; NW-10).

[10] Significantly lower fares have been offered by TWA, Pan Am, and other carriers for brief periods from particular foreign points. (PA-1R-1; TW-1R-1).

included at no extra charge, but frequently a higher fare is charged if Honolulu, Canada, Alaska, Mexico or Puerto Rico are included.[11]

Most "unlimited" travel VUSA fares limit the number of coupons that can be issued,[12] and/or stopovers and connections at a particular city. Many also limit the number of transcontinental flights that can be made. In addition, some have prohibitions against, or blackout periods for, weekend or holiday travel. Virtually all VUSA fares are capacity-restricted according to anticipated load factors on each flight.

Almost all VUSA fares are available only to foreign residents and U.S. military or civilian personnel stationed abroad. Most, if not all, can be sold only in conjunction with the purchase of round-trip transportation to/from the U.S., and many list the participating international carriers.[13] They often are limited to specified foreign origina-

[11]Pan Am, Northwest and a number of other U.S. carriers offer VUSA fares which allow travel to and from Mexico, and/or Canada, as well as between points in the U.S. (PA-1R-1 at 5; NW-1R-1 at 1). These fares are concededly international, and are filed with the Board in international tariffs, as well as with the two governments involved. (I.D. at 3).

[12]In the last several years, the trend has been to limit the number of flight coupons issued under such fares to 12 or less, and to vary the fare depending on the number of coupons offered.

[13]To purchase or use the VUSA fare, the passenger is typically required to show some proof of foreign residence and his transoceanic ticket as both "proof of origin" and, where the fare is thus restricted, the carrier he will use or has used to travel to the U.S. (TW-1R-3, at 1; PA-1R-1, Attachment A; NW-1R-3). A typical "unrestricted" VUSA fare specifies, *inter alia*, that "Passenger at time of check-in must display proof of origin and destination consisting of a round-trip ticket via commercial air [or air/sea] transportation." When a VUSA ticket is issued abroad, the transoceanic ticket is often marked nonendorseable and nonrefundable except upon surrender of all VUSA coupons intact. This appears to be a device to police VUSA fares tied to the international fares of a particular carrier or carriers.

tion points, either by city or by broader geographic area. VUSA fares are sold on separate ticket stock from the international ticket and are technically "nomcombinable."[14] (2 TR 95, 147, 244.)

A few VUSA fares must still be purchased and the itinerary booked outside the U.S. before the travel begins.[15] Increasingly, however, VUSA programs may be purchased in the U.S., at least upon payment of a $100 surcharge, and itinerary changes can almost always be made after arrival in the U.S. for a service charge of $20-25. Many carriers also permit a VUSA passenger, after arrival in the U.S., to purchase a longer period of travel on the previously purchased VUSA fare, or to add an additional point, such as Hawaii, by paying the difference in price. Reservations in most cases can be made at any time prior to the departure of each flight. Generally, changes in flights can be made without charge up to the flight departure, provided that there is no change in the itinerary or routing.

The feature that distinguishes the VUSA fares at issue

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[14]Through baggage handling and other traditional through services are not technically permitted.

[15]Northwest apparently never had such absolute requirements, while Pan Am eliminated them in 1980. (I.D. at 5-6; NW-1R-1.) Capitol apparently eliminated them in 1982, although payment in the U.S. has to be by carrier "miscellaneous charge order." (CL-A, at 5.) Note, however, that purchases after arrival still require both proof of foreign residency and "proof of origin" in the form of the international ticket.

from those that are not[16] is that they are (or at least were) available only to passengers who travel to and from the U.S. on the same carrier offering the VUSA fare, or on a restricted number of other carriers designated as participants. Allegedly not all willing carriers could become participants. The fares at issue were specifically identified in the various complaints filed by foreign air carriers. The complaints challenged the VUSA fares containing this "on-line restriction" on the grounds that (1) for the first time the complainants were precluded from participating in the sale and use of particular carriers' VUSA fares, both by area and by specific market, and (2) in some instances in which they could participate in the VUSA program of a particular U.S. international carrier, it was only through the sale of a higher-priced VUSA fare which was less at-

[16]The VUSA fares of all the U.S. carriers were published in ATP tariff CAB No. 352, the domestic rules tariff. The specific provisions under investigation are:

Capitol	Rule #1058, Visit the USA on Cl.
Northwest	Rule #1022, Transatlantic U.S.A. Pas and Rule #1023, North/Central Pacific U.S.A. Pass.
Pan American	Rule #1030, Visit the U.S.A. on PA, and Rule #1035, South Pacific Visit the U.S.A. on PA.
TWA	Rule #1025, Domestic System Visit U.S.A. Fares, and Rule #1051, Transpacific Visit U.S.A. Fares.

The specific fares that BA complained against are the reduction by TWA of its restricted VUSA fare to $296 in the London (Heathrow)-Philadelphia and London (Gatwick)-New York markets from July 11 until September 6, 1982 and the reduction by Pan Am of its restricted VUSA fare to $299 in the London (Heathrow)-Washington, D.C. and London (Gatwick)-Houston markets from August 12, 1982 until December 15, 1982. Orders 82-8-93 and 82-9-42 denied BA's separate complaints because these fares were simply revisions of fares that were already under investigation and, hence, within the scope of the issues in this case. (I.D. at 4.)

tractive than, or even totally noncompetitive with, the restricted VUSA fare ("two-tier VUSA pricing").

According to the complainants, the on-line restriction was first adopted by Braniff and National in 1979, and was rapidly adopted, along with the related two-tier pricing device, by other U.S. carriers offering international service. Before 1979, the complainants allegedly were able to participate in all VUSA fares on equal terms. The complaints did not challenge the "unrestricted" VUSA fares of any U.S. carrier. Throughout this proceeding, the foreign carriers have maintained this distinction between "restricted" and "unrestricted" VUSA fares, but, as discussed extensively below, the logical implication of most of their arguments is that even the unrestricted VUSA fares open to all willing participant carriers should be considered international for tariff-filing purposes. *See also,* 1 TR 150-151.

Notwithstanding the *Investigation,* VUSA fare offerings have not remained static. In his Initial Decision, the ALJ noted that only TWA and Capitol currently excluded all other carriers from participating in their VUSA programs. By then Northwest permitted four foreign carriers — Qantas, Air New Zealand, CP Air and UTA — to sell its VUSA fare to passengers originating in the South Pacific, subject to the same rules and conditions, including price, as Northwest. (NW-IR-1 at 3.) And he noted that, since February 20, 1981, Pan Am's generally available unlimited travel VUSA fare was available to JAL, Lufthansa and 32 other carriers on the same basis and at the same price as passengers using Pan Am's transoceanic service (PA-R-2, at 3).[17] He might also have noted

[17]Excluding, *inter alia,* its Pacific VUSA fare via Honolulu, which was not available to JAL (FAC-R-5 (rev.)).

that Capitol had opened its VUSA fare to at least one other carrier, Swissair, from Zurich. (CL-A.)

The number of carriers offering VUSA fares, and the number and variety of VUSA fares, appear to be increasing. As of April 1, at least 20 U.S. carriers offered one or more VUSA fares.[18] Most offered from 2 to 7 types of VUSA fares, as well as various prices within each type, depending on such diverse variables as number of coupons (flights), points to visit, group size, place of ticket purchase, point of origin of the international travel, and the identity of the international carrier. The number of individual VUSA fare options is probably greatly in excess of one hundred.

In addition, at least 9 of the carriers offered one or more expressly carrier-restricted VUSA fares.[19] In some cases the number of eligible international carriers is large, reflecting perhaps an "equal availability" philosophy, but in most the number is limited to a few carriers or to the VUSA carrier alone. Several carriers have restricted VUSA fares in markets they do not themselves serve.[20] Some VUSA fares appear to be carrier-restricted in certain markets but not in others. More than a few are available to different carrier groups and/or markets at different prices. While identifying individual carrier-restricted fares

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[18]Air California, Alaska Airlines, American, Braniff, Continental, Delta, Eastern, Frontier, Northwest, Ozark, PSA, and Pan American, Piedmont, Republic, TWA, United, USAir, Western, Wien, and World. ATPCO memorandum tariff, April 1, 1984, and filed VUSA fares which include Canadian or Mexican points.

[19]American, Continental, Delta, Eastern, Northwest, Pan Am, TWA, United and World.

[20]Eastern has a VUSA available only to international traffic of British Caledonian from the U.K. and United has one available to the international traffic of SAS from Scandanavia.

is difficult, given such variations, it appears that as many as 40% of the VUSA programs may contain at least one carrier-restricted VUSA fare. In total numbers, however, the percentage of significant carrier-restricted VUSA fares is much smaller, and the majority of programs are currently unrestricted for all but two of the carriers.[21]

If there is any trend perceivable in VUSA offerings, it appears that U.S. carriers are becoming less restrictive in their general or areawide VUSA fares, while targeting carrier-restricted VUSA fares on a short term basis to specific markets in response to specific competitive situations. (Pan Am brief to Board, at 3.)

B. Use of the VUSA Fares at Issue

The typical VUSA passenger uses an unbundled coach fare or a promotional fare such as an Apex or a Group Inclusive Tour fare to get to the United States (I.D. at pp. 5-7). Seventy-seven percent of Pan Am's VUSA passengers who bought their unlimited milege VUSA tickets abroad started and ended their trip on the VUSA fare at the same U.S. gateway. (PA-6.)

The overwhelming majority of Pan Am, Northwest, and TWA VUSA travelers purchase their VUSA transportation abroad before departing for the United States.[22] Thus, in the vast majority of cases, the passengers planned their VUSA U.S. itineraries before they departed for the

[21]Northwest and United.

[22]Northwest estimates that 80 percent of its VUSA travel is purchased abroad; Pan Am estimates that 96.1 percent of Pan Am VUSA travel is purchased abroad; TWA states that "virtually all" TWA VUSA travel is purchased abroad; and the Capitol Air VUSA originally could only be purchased overseas before the passenger commenced his travel to the U.S. In addition, reservations are usually made for the entire trip when the ticket is purchased. (2 TR 147, 148; CL-1R-2).

United States. This percentage may be declining, however, to the extent that more carriers are permitting VUSA purchases after arrival in the U.S.

Northwest estimates that its VUSA passengers travel, on the average, 3.6 VUSA segments (Northwest IR-1 at 1), although BIA notes that for 22 sample itineraries on Northwest in NW-2, the VUSA passenger traveled an average of 5.9 segments per itinerary; each segment averaged 1,264 miles. Pan Am estimates that its VUSA passengers travel an average of 5.6 segments. (PA-IR-10; 2 TR at 109-110). TWA estimates that its VUSA passengers used an average of 7.7 flight coupons, with an average total VUSA mileage of 6,592 miles. (TW-IR-2, at 1.)

IV. The Contract Rate

In April, 1981, Northwest entered into contracts with two shippers (apparently forwarders) for the carriage of freight between Chicago-O'Hare and Seattle (NW-IR-6). Under these two Contracts, which expired in six months and were not renewed, the shipper received a rate of 6 cents per pound as long as it tendered a minimum of 300 metric tons over the life of the contract. (NW-IR-7.) There was no maximum tender and both shippers met the requirement. The rate level reflected in the Contract equalled a Northwest existing domestic rate (1 TR 64, 70, 71) and the Contracts were subject to the carrier's unfiled domestic cargo rules and regulations. (NW-IR-7.)

The Contracts applied only to shipments ultimately destined to Hong Kong, Japan, South Korea, the Philippines, or Taiwan, moving first to Seattle on a domestic waybill and then moving across the Pacific on a separate, international waybill. The domestic waybill was required to cross-reference the international waybill and attest that

the shipment was "a true international shipment beyond the SEA gateway." (NW-IR-6, at 1.) The concededly international movement beyond the Seattle gateway could be on any U.S. or foreign air carrier, or even by sea, at any applicable international tariff rate (Id.).

At the Seattle gateway, the shipper was entitled to follow normal practice and hold the Contract shipments until enough freight from all sources could be accumulated to form a consolidated international shipment at a preferable international tariff rate. Thus, Contract shipments could be commingled with other domestic-origin traffic at the gateway and the "domestic" and "international" transportation were not necessarily rated at the same time, although the domestic rate was conditioned upon an onward movement at some rate. The Judge found no direct evidence, however, that any of the Contract shipments were delayed or even off-loaded for consolidation at Seattle, finding that Northwest's estimate of an average 24-hour delay did not differentiate the Contract Rate from other domestic-origin cargo. (I.D. at 55; NW-IR-7, at 2-3.)

Northwest concededly instituted these Contract rates to combat the payment by Korea [sic] Airlines and China Airlines of 18 percent commissions for transpacific international traffic. These commissions were diverting Chicago-West Coast traffic away from Northwest (NW-IR-7; 1 TR 68). At that time Northwest was paying 5 percent commisions on its whole system for international shipments (1 TR 82). Another acknowledged purpose of the Contract rates was to offset the practice of discounting tariff rates that was common during this period in the Chicago area, and which had been affecting Northwest's traffic. (NW-IR-7.) No other similar contracts have been entered into by Northwest.

V. The Tariff-filing or "Definitional" Issue.

The most extensively argued issue in this case is whether the "carrier-restricted" VUSA fares and the "export-restricted" Contract rate at issue are domestic or international for tariff-filing and review purposes under the Act and the relevant bilaterals. The foreign carriers contend that they are, as a matter of traditional legal interpretation and current statutory policy, in "foreign air transportation" as defined in section 101(24) of the Act and, consequently, must be filed with the Board under section 403, and with the foreign governments involved under the bilateral agreements and section 1102. The U.S. carriers claim that they are in "interstate air transportation" for similar legal and policy reasons, and, along with BIA and DOT, argue that they need not and should not be filed with the Board or with any foreign governments.

A. The Initial Decision

In approaching this issue, the ALJ focused on the Board's request for a detailed factual analysis of "how the restricted VUSA fares are actually applied."[23] He found that the Board's definitional standard was set forth in the *Tariff Flexibility Rulemaking,*[24] and the order instituting

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[23]I.D. at 14, 27, citing Order 81-11-182 at 8, and Order 81-11-58 at 7.

[24]Citing ER-1246 at 11: "The term 'foreign air transportation' as currently understood for the purposes of filing requirements under the Act and bilateral obligation is much more limited. It clearly covers tariffs for *through fares for on-line service, joint fares for interline service and arbitraries used to construct interline fares to interior U.S. points.* Such fares would not be affected by our rule and their filing will continue to be mandatory. Between such tariffs and purely domestic fares there may be fares that raise uncertainties; these are best analysed on a case-by-case basis and in a specific factual context." [Emphasis added.]

this investigation, particularly the Board's directive that the parties "provide comprehensive factual evidence as to whether the fares as actually applied are typically part of a continuous integrated international journey originating and terminating in a foreign country." (I.D. at 14.) He interpreted these directives broadly. In essence, he saw his task as that of deciding whether, on balance, the restricted VUSA fares are more like domestic fares which are not filed, or more like the traditional "through fares . . . joint fares . . . and arbitraries . . ." referred to in the *Tariff Flexibility Rulemaking.*

Applying this standard, he rejected the foreign carriers' "strict interpretation of the 'flow of commerce' theory which provides that the characterization of transportation as foreign or domestic is determined by the intent of the shipper or passenger at the outset of the journey and is not affected by the occurrence of stopovers or other breaks in the transportation." (I.D. at 15.) He found that the Board has rejected such a mechanistic approach and instead considers subjective passenger intent or flow of comerce to be only one factor to be considered in the classification of traffic.[25] He found no inconsistency between this view and earlier Board decisions, some of which were cited by the

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[25]I.D. at 15-17, citing the orders instituting this case and ER-1246. In the later proceeding, the ALJ noted, the Board squarely rejected similar arguments by IATA that Board precedent required that the ultimate origin and destination be used to define transportation as foreign or domestic. The Board stated, *inter alia,* that "[i]n fact, we have rejected that test when necessary to preserve a fundamental policy of the Act." ER-1246 at 12.

foreign carriers in support of the strict flow of commerce test.[26]

He also rejected the foreign carriers' related assertion that the Board has always considered fares applicable between foreign points which *can* be combined with fares to or from U.S. points to be fares in "foreign air transportation," and hence must find the restricted VUSA fares *a fortiori* in foreign air transportation. The IATA agreement cases cited by the foreign carriers, he found, do not support their premise. Rather, the Board's exercise of its regulatory jurisdiction in such cases as *IATA Europe-Israel Passenger Fares Proceeding,* Order 78-7-113, was based on the effect of the IATA agreements on U.S. commerce, not on the scope of statutory or bilateral tariff-filing requirements. Thus, he found, the Board has never required IATA carriers to file fares for transportation that is solely between two foreign countries. Such fares are not considered to be for "air transportation" under the Act unless they are part of a through trip to or from the United States. The Board has emphasized that "absent agreements or other antitrust implications, . . . , we do not have jurisdiction over every foreign air fare a U.S. citizen may use or seek to use." (Order 79-2-130 at 5.) Combinable fares, he concluded, may affect foreign commerce under section 412, but the transportation under them does not

[26]*E.g., Qantas Empire Airlines Limited Foreign Transfer Traffic Case,* 29 CAB 33 (1959); *Colonial Airlines, Inc., et al. Atlantic Seaboard Operation,* 4 CAB 633 at 634 (1944); *Sitmar Cruises, Inc.,* Order 75-8-88 (1975); and *Canadian Colonial Airways, Inc., Montreal-Nassau Service,* 2 CAB 752 (1941). Similarly, he found no overriding support for a strict flow of commerce test in various ICC cases cited by the foreign carriers, *e.g., Baltimore & OSWRR. Co. v. Settle,* 260 U.S. 166 at 173 (1922) and *Chicago, Milwaukee & St. Paul Ry. Co. v. Iowa,* 233 U.S. 334 (1913), although in any event he would not give them controlling weight over Board cases. I.D. at 18, note 17, and at 20, note 18.

automatically become foreign air transportation under section 403 and the tariff-filing requirements of the bilateral agreements. (I.D. at 18-20.)

The ALJ began his factual analysis by observing that "the VUSA fares at issue in this proceeding are novel and the resolution of their status as international or domestic has not been considered by the Board in any previous proceeding. On examination, they contain characteristics of both foreign and domestic fares." Historically, he noted, VUSA fares have been considered domestic for U.S. tariff-filing purposes, and it does not appear that any foreign government ever questioned their status. At the same time, the carrier restrictions at issue only date from about 1980.[27]

The ALJ next rejected the argument of the U.S. carriers and BIA that, since VUSA fares cover only travel within the U.S., they are not international, but are for interstate air transportation under section 101(24) of the Act. He concluded that this overlooks (1) the fact that VUSA fares can be purchased only by residents of foreign countries; (2) the fares at issue require the traveller to use the transoceanic service of the VUSA carriers; and (3) one of the primary reasons for instituting the restricted VUSA fares

[27]I.D. at 20-21. In response to Order 81-11-182 at 8, Pan Am cited three VUSA-type fares offered in Brazil, France and India as direct evidence that foreign carriers and governments also consider such fares to be "domestic" only. The ALJ found that "[u]nlike the VUSA fares at issue, none of these fares contain a restriction against participation based upon the carrier the passenger used for the transocean travel. (2 TR 137) . . . No party offered any evidence concerning any VUSA-type fare which may be offered in Germany or Japan and which may contain restrictions similar to the VUSA fares at issue." (I.D. at 13.)

was to attract passengers to the VUSA carrier's international service.[28]

The ALJ gave great weight to the foreign carriers' argument that the VUSA fares are in reality international arbitraries used to construct through fares to interior U.S. points. Starting with the tariff definition of arbitrary,[29] he agreed that the distinguishing feature of an arbitrary is that it is a fictitious or "paper" fare not available for purchase as published, and that the same is true for the VUSA fares. He found that "[e]ven though VUSA fares were published in a domestic tariff, they are not independently available for purchase; it [sic] can only be purchased in combination with an international trip on the transatlantic VUSA carrier." (I.D. at 23.)

The ALJ acknowledges that the VUSA fares are unlike "traditional point-to-point arbitraries" in that they cover transportation exhibiting unlimited mileage, multiple stopovers, circuitry of routing, and no readily identifiable turnaround point, as the U.S. carriers, BIA, and DOT have argued. Nevertheless he concludes that these differences have not been shown to be material to any Board criteria for distinguishing domestic from international fares. He found that the VUSA fares at issue are "fares covering a through international journey, and are undistinguishable from arbitraries covering beyond gateway transportation." (I.D. at 23-24.) He amplified the basis for this conclusion by finding that the multiple stopovers

[28]He qualified this latter finding with the statement that "VUSA fares also have beneficial effects on the U.S. carriers' domestic system. But this is not the sole purpose for instituting the restricted VUSA fares." (I.D. at 21-22.)

[29]"Arbitrary means an amount published for use only in combination with other fares for the construction of through fares. It is also referred to as 'Proportional Fare', 'Basing Fare', and 'Add-On Fare.'" Tariff CAB No. 376, 6th revised page 2, effective July 26, 1982.

engaged in by VUSA travellers do not amount to a factual and legal "break" in the passenger's journey between their international and VUSA travel because they "are planned stops in the VUSA traveller's itinerary, and the itinerary was planned prior to his departure from his origination point." Thus, they do not alter the fact that the VUSA traveller "is engaged in an integrated journey from a foreign point through the United States and back to his origin point." (I.D. at 25.)

The ALJ also dismissed BIA's related argument that VUSA passengers use the fares for domestic excursion travel much as they would use other acknowledged domestic fares on the grounds that (1) aside from an Eastern excursion fare (3 TR 23), no exhibit or witness cited any domestic fares that offer the VUSA features of unlimited mileage, multiple stopovers and circuity of routing, and (2) even if it could be found that domestic discount fares would be used if VUSA fares were not available, this fact does not transform VUSA fares into domestic fares any more than the equally logical proposition that passengers would rely on point-to-point domestic discount fares if international arbitraries were not available transforms such arbitraries into domestic fares. (I.D. at 25-26.)

In what appears to be a general summary of the factors underlying his conclusion on the definitional issue, the ALJ concluded that VUSA fares

> . . . may not be exactly like traditional international arbitraries, but they are very close. The restricted VUSA fares under investigation can only be purchased in combination with an international trip on the VUSA carrier. The VUSA program is restricted to the foreign nationals and cannot be purchased by the general public for transportation within the United States. More-

> over, the overwhelming majority of VUSA tickets and itineraries are purchased and prepared at foreign origination points. Finally, VUSA fares are international fares because the intent of the passenger in purchasing the VUSA fare was to engage in an international roundtrip journey, and that was the intent of the carriers offering the VUSA fare. (I.D. at 24-25.)

The fact that VUSA revenues are classified as domestic for international revenue accounting purposes, and that they are ticketed separately on domestic ticket stock does not, in the ALJ's view, "detract from the fact that VUSA fares are part of an integrated international journey." He found such evidence largely "self-serving" and in any event not previously relied upon by the Board as a basis for determining whether a fare is international or domestic.[30] He emphasized that "the restricted VUSA fares at issue can only be purchased by a passenger who holds a trans-oceanic ticket from the VUSA carrier." (I.D. at 26.)

Noting that Northwest, BIA and DOT argue that VUSA fares must be found to be domestic in order to achieve relevant policy goals of the Act, the ALJ concluded without elaboration, that

> While such considerations are important, the evidence of record does not provide any substantial basis to find that those policy goals will be hindered by a determination that the restricted VUSA fares are in foreign air transportation.

[30]In this context he cites a BIA witness's acknowledgement that "a domestic fare combined with an international fare causes the transportation to be international." I.D. at 26. However, the quote at 3 TR 61 was limited by the witness to fares combined "on the same ticket."

> The fares at issue are not all VUSA fares, but only the restricted VUSA fares of Northwest, Pan Am, TWA, and Capitol. Finding these fares to be international does not mean that discrimination by foreign governments will become the rule for VUSA fares as the U.S parties appear to imply. (I.D. at 27.)

Finally, he emphasized that "the VUSA fares at issue are distinguishable from the fares at issue in the *Tariff Flexibility Rulemaking*, ER-1246, in that (1) the latter, unlike VUSA fares, were "generally and independently available for purchase by domestic passengers without reference to prior or subsequent travel on international flights," and (2) "the impact of the restricted VUSA fares is in the marketing of the U.S. carriers' transoceanic service." (I.D. at 27.)

The ALJ concluded that the export-restricted contract rate is in foreign air transportation for tariff-filing purposes chiefly on the ground that "it is clear that the intent and effect of the contract rates was to enhance Northwest's competitive position in an international market." (I.D. at 53.) He emphasized Northwest's concession that the rate was a competitive response to a change in the commission structure of several foreign air carriers, not domestic competitors, and also its statement in an internal document[31] that the rate was for "transpacific rate construction purposes" which would allow competitive pricing without changing its filed discount rate structure or discounting off filed rates. He rejected Northwest's contention that there was a legal and factual "break" in the transportation at Seattle, finding that there was no evi-

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[31] The document, NW-IR-9, was accorded confidential treatment by the ALJ under Rule 39, except for those portions quoted in the I.D.

dence of actual off-loading, consolidation, or delay of Contract rate shipments. He also concluded that the rate "is really an arbitrary or an add-on" to an international rate, since it is "for use only in combination with" such rates "for the construction of a through rate to the Orient." (I.D. at 56-67.)

B. Discussion of Parties' Positions on Review

Reflecting the diverse positions of the parties, the ALJ's filing analysis combines a number of traditional and arguably novel criteria including (1) flow of commerce (passenger intent), (2) nature of the transportation (passenger use), (3) availability restrictions (analogy to "arbitraries") and (4) primary economic and competitive impact (carrier intent). Not surprisingly, each party on review would at least modify the focus of his analysis, if not its actual application and conclusion.

British Airways supports his analysis generally, but would have the Board emphasize that it has essentially adopted a comparative interest analysis that focuses on whether the "economic impact" and the "competitive significance" of an innovative fare is primarily domestic or international, and whether the fare is promoted actively and exclusively to international traffic. We agree with BA and the ALJ that economic impact, competitive significance and competing regulatory interests must be weighed directly in this case because we find that the more traditional traffic — and transportation-oriented criteria are either inconclusive or would lead to absurd results under our statute and previous decisions. At the same time, we attach little importance to "whether a fare is promoted actively and expressly to international traffic." If foreign sales and itinerary planning were a material factor for filing purposes, as the ALJ found, both

unrestricted VUSA fares and many combinable foreign country and domestic discount fares would be international as well, a result at variance with both U.S. and international tariff filing practices.[32] Finally, we emphasize the point made by DOT and Pan Am on review that many domestic fares and practices – including any fare that is combined with a foreign fare – have an "international impact." For such a factor to be of decisional significance for filing purposes, the international impact must be more than incidental. It must reflect the economic and competitive essence of the fare. ER-1246, Order 81-7-108.

JAL and Lufthansa support the ALJ's conclusion with regard to the filing of the fares and rate at issue, but continue to emphasize the primacy of three criteria, each of which would render international many fares and rates now considered domestic by the Board and under international practice. They contend that (1) the Board is bound to apply the traditional "flow of commerce" theory, under which the characterization of transportation as foreign or domestic is determined by the intended ultimate origin and destination of the shipper or passenger at the outset of the journey, and is not affected by the occurrence of stopovers or technical distinctions in fares, such as separate tickets; (2) the Board has always considered fares applicable between two foreign points which *can* be combined with fares to or from the United States to be in "foreign air transportation" and hence must reach the same conclusion with respect to fares and rates between United States points which *must* be combined with fares to and from the United States; and (3) the fares

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[32]The Board has not required the filing of foreign domestic fares sold in the U.S., even when used in conjunction with an international trip. It has never considered sales in the U.S. to raise a sufficient regulatory interest to justify such an interpretation of section 403 or the tariff-filing provisions of the bilaterals.

and rate are legally indistinguishable from traditionally filed international arbitraries in that they are nothing more than amounts to be used in combination with international gateway-to-gateway fares or rates to construct through international prices.

As discussed further below, the ALJ correctly rejected the first two contentions, but incorrectly found the fares and rate at issue to be legally indistinguishable from international arbitraries. We reject his analysis and conclusion on the latter point for three major reasons. First, he gave insufficient weight to the technical differences between the fares and rate themselves and the international transportation to which they are tied for marketing purposes, while finding, without direct or adequate evidence, that the former cover a "through international journey." Second, his definition of an arbitrary, as evidenced by his findings, would encompass not only all VUSA fares but also, quite probably, many combinable domestic fares and rates as well. And third, by focusing only on flow of commerce and other traffic- or transportation-oriented factors, he ignored the major economic and competitive distinctions between the export-restricted Contract rate and the carrier-restricted VUSA fares.

BIA, DOT and the U.S. carriers challenge the ALJ's result on factual, legal and policy grounds, contending that he ultimately ignored overwhelming record evidence that the fares are structured and used as separate domestic fares, basing his decision instead on "availability restrictions" which are legally irrelevant to the tariff-filing issue.

While their arguments vary somewhat in emphasis, they all make the same basic case: (a) the Board has made it clear that the traditional "flow of commerce" test is not controlling; (b) the Board has not required the filing of

combinable foreign country fares unless actually combined on a single "through" ticket; (c) the VUSA fares and the international roundtrip tickets to which they are tied for marketing purposes are technically distinct transportation packages (*e.g.* separate ticket contracts, separate points served, separate terms and conditions, independent adjustability of schedules and itineraries, and absence of "through" services such as baggage checking), and hence, on their face, are distinguishable from traditional through fares, including international add-ons and arbitraries; (d) the Board has essentially adopted an "actual use" test for innovative fares such as these that may not meet all traditional criteria, and the record shows that the VUSA fares at issue are used for qualitatively distinct and separate domestic travel, which begins and ends at the gateway and which is distinguishable in purpose and nature from travel under conventional through fares, including international add-ons and arbitraries; (e) the availability restrictions to foreign residents and to the purchase of an international ticket, while unusual, do not outweigh the distinctiveness of the services or the change in the way the passenger uses the fares, while the on-line restriction and such factors as the carrier's motives in establishing the fare and its economic and competitive impact are relevant only to the "fair opportunity to compete" issue, not to the fare's filing status, and (f) the ALJ's decision would reverse longstanding international and Board practice regarding control of domestic discount fares, would undermine the Board's statutory deregulation mandate upheld most recently in ER-1246, and would cast doubt on the status of numerous fares not at issue, as well as the validity of fare construction practices and policies of major importance to the Board.

We agree with some of these contentions, noted below,

and with their general criticism that the ALJ's decision is overbroad. However, we find their "actual use" test to be factually inconclusive as a means of resolving the filing status of the fares and rate at issue. As a filing test it has the additional disadvantage of providing little or no guidance to carriers or government for future cases. Moreover, we do not agree that the "availability restrictions," or marketing ties to foreign travel and to particular carriers, are irrelevant to the definition of the fares and rate for filing purposes. They may raise issues under other provisions of the bilaterals as well, but to ignore the economic and competitive essence of the restrictions in a close case such as this would be to exult form over substance and undercut, at least to some extent, the purposes of the international tariff-filing mechanism.

In our view, neither the ALJ nor any of the parties has provided a wholly satisfactory filing test for dealing with the types of fares and rates at issue. All of the analyses fail, for one reason or another, to differentiate the fares and rate at issue from other fares and rates on the spectrum from "domestic" to "international." That spectrum, described in the *Tariff Flexibility Rulemaking* and in the Initial Decision before us, ranges from "combinable" domestic fares and rates, on the one hand, to traditionally filed "through" fares and rates, on the other.

C. Disposition

As we implied in the instituting orders and in ER-1246, this is a limited case, and one essentially of first impression. It concerns a species of purportedly domestic fares and rate which has most of the earmarks of being a separate transportation package (with separate tickets or waybills, separate terms and conditions, separate points, and separate services), but which is expressly tied for mar-

keting purposes to international travel. The VUSA fares at issue, moreover, are a subset of such fares and rates. Their availability is not only tied to the purchase and use by foreign residents of round-trip travel to and from the U.S., but is also tied to international travel on a particular carrier or carriers.

The ALJ correctly noted the novelty of the fares and rate at issue, and was essentially correct in concluding that the carrier-restricted VUSA fares "contain characteristics of both foreign and domestic fares." (I.D. at 20-21.) However, his analysis lacks a unifying rationale, and the breadth of most of his criteria and findings would also support the filing of fares and rates which are not directly at issue and which he apparently (and we certainly), would not consider to be fileable. This is particularly true of the "unrestricted" VUSA fares, which he found to have been considered domestic for filing purposes by U.S. carriers and historically accepted as such by foreign governments. The key finding throughout his analysis is really two separate findings: first, that the purportedly domestic travel is tied to specific international travel in a manner suggesting a continuous journey and, second, that both domestic and international travel must be on a specified carrier or carriers. The second element is essential to his test if he is to distinguish, as he apparently does, between the VUSA fares at issue (originally all carrier-restricted) and those not at issue (similarly tied to the specific round-trip international travel, but on any carrier). Yet he never expressly made this distinction in his analysis of the VUSA fares, and he also found the Contract rate to be international, even though it was not carrier-restricted. The implicit distinction does draw support from his finding that the primary purpose and impact of the fares and rate at issue is to attract passengers to the international services of the offering carriers, but this finding is overbroad in terms

of the record and its generality could encourage challenges to other domestic fares or practices on grounds of their alleged "international impact." Moreover, the finding is plainly incorrect in the case of the Contract rate.

Our reasons for selecting the carrier restriction as the deciding factor for filing purposes in this case can best be explained through a closer look at the Initial Decision and the positions of the various parties.

As a threshold matter, we agree with the ALJ and the foreign carriers that the fares and rate at issue and, indeed, all VUSA fares, are distinguishable from the typical "combinable" domestic fares which were the focus of the *Tariff Flexibility Rulemaking,* in that they are not "generally and independently available for purchase by domestic passengers without refernce to prior or subsequent travel on international sectors." In ER-1246, and in Orders 81-9-96 and 81-11-58, we rejected most of the arguments made here by the foreign carriers and concluded that all fares available on their face to purely domestic passengers cannot be filed in international tariffs regardless of how they may be used for construction purposes. We re-affirm those findings and conclusions here.

At the same time, however, there is nothing in the *Rulemaking* to suggest that the distinctions presented here by the marketing ties to foreign travel generally, or to particular carriers, necessarily requires a different result. ER-1246 merely recognized that the fares and rate at issue raise questions to be resolved on the basis of a full record. Indeed, there is nothing in the language of ER-1246, section 403, or any of the relevant bilaterals which *requires* a result one way or another on this issue. Both the U.S. and foreign carriers have made "plain meaning" arguments

and all must be rejected in favor of a factual, legal and policy analysis.[33]

The touchstone of section 403, the traditional definition of an arbitrary, and Board precedent on the scope of tariff filing, is whether a "through" fare is involved. But this key concept has never been precisely defined. As discussed below, we agree with the ALJ and the foreign carriers that the general tie to international travel which characterizes all VUSA fares and the Contract rate does raise some uncertainties in distinguishing "through" fares for filing purposes, at least in some cases. We conclude, however, that this marketing tie does not, by itself, make the VUSA fares or the Contract rate international for filing purposes. At most it makes such fares and rates a closer case under some of the more traditional criteria considered by the ALJ and the various parties. To the extent that the line between some or all of the tied fares and traditionally filed "through" fares is less clear, we must rely more on potentially broader but more substantive economic criteria.[34]

[33]In particular, the carriers contend that the fares and rate at issue fall literally within the definitions of "interstate" and "foreign" air transportation. Both cannot be true. If either were, this case would not have been necessary. In addition, we reject the assertion of the foreign carriers that the fares and rate must be filed in international tariffs because the transportation thereunder is part of the "public transport" between the U.S. and other countries or at least is "ancillary" to the "public transport" under provisions such as Article I (m) of Bermuda II. "Ancillary" was intended to cover incidental services such as those for excess baggage or pickup and delivery, not to broaden the fares covered by "pubiic transport." As for "public transport," the language of the tariff-filing provisions is quite general and certainly does not require such an interpretation.

[34]In Order 81-11-58, for example, we indicated our intent to "retain generally accepted distinctions between foreign and domestic air transportation." However, as British Airways observes, we also clarified our willingness to weigh economic factors and competing regulatory interests where such an analysis is necessary to resolve ambiguities under traditional criteria.

As British Airways acknowledges, such criteria indicate that the tied fares and rates are essentially domestic in every meaningful sense. It is only when they are also carrier restricted as to international travel that they present a risk that they are no longer economically and competitively independent of the international fare to which they are tied. This basic distinction is reflected in the general treatment of unrestricted VUSA-type fares by carriers and governments,[35] and in the complaints against the particular VUSA fares which prompted this proceeding.

We fully concur in the ALJ's rejection of two of the positions taken by JAL and Lufthansa. First, he correctly found no precedent for their argument that the Board has in fact acknowledged both combinable and even noncombinable fares between foreign points to be in "foreign air transportation" for tariff purposes by asserting substan-

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[35]VUSA-type fares of the "unrestricted" variety for travel in their home country have been and increasingly are being offered in the U.S. by foreign carriers (*i.e.*, fares available only in conjunction with round-trip travel from/to the U.S.). Allowing for the influence of the present case on recent filings, such as those by British Airways and British Caledonian, the record supports the conclusion that such fares, as well as the Discover America and other unrestricted VUSA fares offered by U.S. carriers, have been treated as domestic for filing purposes by most countries, at least so long as the potential travel under the fare is entirely within one country. The Board has accepted for filing purposes VUSA fares permitting stopovers at one or more points in Canada or Mexico, for example, and these are concededly filed with those governments as well. The filing treatment of carrier-restricted fares and rates is less clear, largely because, as the ALJ found, there is little direct evidence that foreign carriers have offered them. However, the Board itself has accepted for filing Continental's on-line restricted "Koala" excursion fare (Order 82-6-156) and its on-line "$90 arbitrary" (Order 83-7-73).

tive jurisdiction over them.[36] And second, he correctly rejected the "strict flow of commerce" theory which they also continue to emphasize on review. As he found, the Board has never given unqualified acceptance to an origin-destination test, and its limited consideration of passenger intent in other statutory contexts was to aid in determining whether there was a significant "break" in the journey. Where another test, such as a carrier's geographic operations, was more relevant to the statutory provision and policies at issue, flow of commerce principles were readily rejected. *Qantas Empire Foreign Transfer Traffic Case*, 29 CAB 33 (1959). The *Qantas* principle is controlling here. In ER-1246 and Order 81-11-58, we fully considered IATA's identical arguments in both the statutory and bilateral contexts, and concluded that, for tariff filing and review purposes, "the intent of a passenger obviously cannot control the determination of whether the air transportation provided is foreign or domestic." Its application here would be inconsistent with that decision and equally arbitrary in result. It would render international not only all VUSA fares, but all combinable domestic fares as well.

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[36]The board has not required the filing of combinable fares between foreign points, whether within one country or even in two or more countries, unless they are actually combined on a single "through" ticket. ER-1246, at 11-12; I.D. at 18. Moreover, in the IATA Europe-Israel Fares case, Orders 781-7-113 and 79-2-130, the Board made it clear that the foreign discount fares at issue were not in "air transportation" and need not be filed with the Board. The Board's disapproval of the IATA agreement was based on its section 412, not its section 403 authority, and its target was not individually noncombinable foreign fares. And finally, cases such as TWA v. Lufthansa and Air India Fares, Orders 81-2-68, 81-7-160 and 81-10-67, involved the issue of interline matching rights to the foreign gateway, *i.e.*, the assertion of regulatory jurisdiction over concededly international travel. No tariff-filing issue was presented.

We therefore agree with BIA, DOT and the U.S. carriers that the ALJ erred in relying on a finding that the intent of the typical VUSA passenger is to engage in an international round-trip journey. Passenger intent sheds little, if any, light on the policies involved in the tariff question presented here. Moreover the ALJ based his finding on other findings that most VUSA fares are sold abroad and most itineraries are initially planned abroad. The anomaly of domestic purchases aside, his inference [sic] unsubstantiated. Separate "side" trips within the U.S., using generally available domestic fares, are also sold and planned abroad. The ALJ's finding in fact would apply with equal force to all VUSA fares and, indeed, to all combinable fares used by double-ticketing passengers. It is in reality an application of the "strict" flow of commerce theory he rejected. Finally, we agree with BIA, DOT and the U.S. carriers that the evidence of record concerning the actual usage of excursion VUSA fares provides at least as much support for the conclusion that typical VUSA passengers consider VUSA travel to be a separate trip, with a legal and factual "break" in the journey at the U.S. gateway.[37]

[37]In BIA-R-2, BIA examined the routing used and the cities visited by the passengers using the 22 actual itineraries supplied by Northwest (NW-1), the sample itineraries of TWA (TW-IR-2), the "hypothetical" itineraries compiled by Lufthansa in FACT-T-1 and the itinerary of Northwest used by JAL in FAC-T-2. According to BIA, the data show that, in practice, the routings used on most of the itineraries are quite indirect and circuitous, involving up to 50 percent more mileage, and often involve multiple connections and backhauls. Such indirect routings impose penalties of time and inconvenience on the passenger, not to mention the tedium of multiple connections. Passengers assertedly would not undergo such circuity if the VUSA fares were being used for point-to-point through travel. Similarly, the large average number of segments flown by the passengers, the high average length of haul per segment, the average total mileage per VUSA passenger, the number of stopovers made, and the length of the VUSA passenger's stay all reinforce the conclusion that VUSA travel is a separate trip, not a series of segments of an integrated international journey. O.B. at 11-12.

There is, in fact, no direct evidence in the record to support the ALJ's finding that the VUSA passenger is engaged in a continuous, integrated international journey in any traditional sense.

The difficulty of resolving the definitional issue in this case through recourse purely to criteria which focus on the "nature" of the traffic or the transportation, as defined by the presumed intent or actions of the user, is highlighted by the controversy over whether the fares and rate at issue are distinguishable from international arbitraries and other traditionally filed through fares. The ALJ agreed with the foreign carriers that they are legally indistinguishable from filed arbitraries and add-ons in that they too are essentially an "amount published for use only in combination with other fares for the construction of through fares." BIA, DOT and the U.S. carriers disagree, contending that the record on actual passenger use of the VUSA fares shows that they are used in the same manner as combinable domestic fares, are not part of an integrated international journey, and are not used as disguised "add-on" fares. Northwest and BIA make similar arguments with regard to the Contract rate.

Their primary argument is that there are fundamental differences between "typical" travel on arbitraries and other through fares, and "typical" travel on VUSA fares. The principal disadvantage to such an analysis is that, as a predominantly factual test, it does not seem to fit all the facts. In particular, the emphasis on actual use does identify certain differences between *excursion* VUSA travel and typical travel on international through fares, such as unlimited mileage, multiple stopovers, circuity of routings and lack of a definable turnaround point,[38] but, as the

[38]On the other hand, excursion VUSA travel would seem to be equally distinguishable from typical domestic discount fares. BIA's

foreign carriers note, it does not distinguish the point-to-point or single segment VUSA fares, such as Capitol's. These remain elusively difficult to distinguish from add-ons and arbitraries under BIA's factual analysis.[39] Similarly, as the ALJ found, there is little evidence on the actual use of the Contract rate at issue and thus finding a "break" in the transportation on that basis alone would be quite tenuous. In general, the ALJ, JAL and Lufthansa also argue persuasively that a legal filing test based essentially on differences in "typical" travel patterns would seem to be inherently uncertain and subject to controversy. It would provide almost no guidance for the classification of other fares and rates.

While the "actual use" analysis is inconclusive in providing a general functional distinction between all VUSA fares and export rates, on the one hand, and traditionally filed add-ons and arbitraries, on the other, we agree with BIA, DOT, and the U.S. carriers that the formal characteristics of the fares and rates themselves provide a number of significant and traditionally recognized distinctions from through fares. On their face they are distinct transportation packages, involving *inter alia,* separate ticket or waybill contracts, service between separate points, separate (and differing) terms and conditions, separately

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argument that excursion VUSA fares are closer in use to domestic fares is inconclusive as a matter of fact and logic.

[39]For example, it would appear difficult to distinguish Capitol's VUSA fare, which these parties would not file, from Continental's $90 arbitrary described in Order 83-7-73, which was filed. Moreover, Continental's "Koala" excursion fare, described in Order 82-6-156, was also filed, and it also would be difficult to distinguish from many unfiled excursion VUSA fares. The point is not whether these fares were correctly filed, but that reasonable people could differ on a particular case if the analysis is limited to the criteria emphasized by BIA and the ALJ.

adjustable schedules and itineraries, and absence of "through" services such as baggage checking. As these parties point out, traditional arbitraries share few, if any, of these formal characteristics. In particular, we believe that the use of separate tickets or waybills is a material distinction from add-ons and arbitraries. We agree with the ALJ that it may not be determinative of the filing issue in this case, but we are unable to agree that it is without traditional or current significance. The use of one or multiple tickets has been a consistently noted distinction in past Board cases. Each ticket or waybill is a separate contract, and the terms and conditions of transportation (as well as availability) frequently differ. Each user is on notice when the carrier issues two separate contracts that through services may not be available. As BIA emphasizes, availability and combinability are not synonymous.

Finally, these parties emphasize that arbitraries and add-ons are merely tariff construction mechanisms whose only function and purpose is to compute a single through fare on a single ticket; they have no independent existence from a consumer standpoint.[40] VUSA fares, they argue, are independent in every respect except availability of purchase.

The ALJ gave little or no weight to these formal, largely carrier-controlled characteristics and distinctions. He found that the literal definition of an arbitrary fits the VUSA fares at issue in that (1) they are not independently available for purchase and (2) they are fares covering a through international journey. We agree with BIA, DOT

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[40]BIA observes that the add-ons proposed by World Airways in the *Boston-London Exemption Case*, Order 80-5-8, cited by the foreign carriers, were not separately issued tickets, but rather were "predetermined amounts used to construct a single through fare on a single through ticket."

and the U.S. carriers that his supportive findings[41] do not distinguish the carrier-restricted VUSA fares from other VUSA fares or, in most cases, from combinable domestic fares, and that, as indicated above, his key finding that the fares cover a through international journey is fundamentally an unsupported assumption.

The lack of evidence supporting his finding of a through journey is the principal flaw in the ALJ's analysis of the through-fare analogy in purely traditional terms. The defect is even more apparent in the case of the Contract rate. It led him to reject a number of consistently-recognized features of the fares and rate at issue which could support their classification as "domestic" under Board precedent and general international practice. Thus, while the general marketing tie to international transportation admittedly creates some uncertainty in the application of traditional traffic and transportation-oriented criteria, and in the weighing of the formal characteristics of the transportation documents themselves, we conclude that, even under a traditional or formalistic analysis, the tie to separately ticketed foreign travel alone does not justify the classification of any of the fares or rate at issue as international for tariff filing and review purposes.

While the parties vigorously dispute the filing status of the fares and rate in terms of these various formal and

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[41]He found the fares to be "very close" to international arbitraries because (1) they can only be purchased in combination with an international trip on the VUSA carrier; (2) they are restricted to foreign "nationals" (residents) and are not available to any purely [sic] itineraries are purchased and prepared at foreign origin points; (3) the overwhelming majority of VUSA tickets and itineraries are purchased and proposed at foreign origin points; and (4) the intent of the passenger in purchasing the VUSA fares was to engage in an international roundtrip journey and that was the intent of the carrier offering the VUSA fare.

traditional criteria, there is very little actual disagreement that the carrier restriction itself, as contrasted with the general marketing tie to foreign travel, does raise some significant economic and competitive concerns. The ALJ found that one of the primary reasons for instituting the restrictive VUSA fares was to attract passengers to the VUSA carrier's international service, and he listed this as at least one factor in his decision that such fares are international for filing purposes. On review, BIA, DOT and the U.S. carriers point out that the ALJ qualified this finding with another, that restricted VUSA fares also have beneficial effects on the U.S. carrier's domestic system, but they made little effort to dispute his basic point. Rather, they argue that the economic and competitive issues implicit in such a finding are properly to be considered only in the context of the bilateral guarantee of a fair opportunity to compete, not in the tariff-filing context. DOT, for example, expressly agrees with BA that the marketing and competitive implications of the restricted VUSA fares are "primarily international," but it then asserts that the only relevant filing test under ER-1246 is the "nature of the transportation" itself. Similarly, BIA states that the on-line restriction is without legal significance for filing purposes because there is no basis for concluding that a journey is any less a through international journey because it is interline rather than on-line.

The basic response to both positions is that the issue is not simply whether a through journey is involved but whether, in light of all the circumstances, a through fare is involved. It is the fares that must be classified for filing purposes, and that determination need not be limited to traditional "journey" criteria where they are inconclusive. ER-1246 did not define what a "through" fare is, but there

is no indication that the Board contemplated the elevation of form over substance.

D. The Board's Test

In resolving this case we must strike a fair and reasonable balance between the competing, but legitimate, regulatory interests of both the U.S. and foreign governments. Accordingly, we must focus on the basic purpose of the Airline Deregulation Act, which is to deregulate essentially domestic fares, and on the basic purpose of any bilateral tariff-filing requirement, which is to provide formal review and approval procedures in the case of essentially international fares.

We believe that the carrier restriction is the line which permits us to harmonize these basic considerations in this case. The marketing tie to foreign travel alone does not make a fare or rate "international" in any fundamental economic sense. The pleadings and the record make it abundantly clear that a fare or rate between domestic points which is available only in conjunction with foreign travel may nevertheless be rational *domestic* pricing behavior on the part of the offering carrier. The purpose of such a marketing restriction, as the Board observed in its initial approval of Discount USA fares in 1968,[42] is to generate traffic and revenues for domestic services by offering a special low fare to highly price-elastic foreign residents without diluting revenues from purely domestic

[42] *Discount USA Fares*, 48 CAB 892 (1968).

traffic.[43] The Board found such a restriction to be not unjustly discriminatory because of the economic benefits involved.[44] As BA and the other foreign carriers have indicated throughout this proceeding, they agree that unrestricted VUSA fares have a domestic economic validity while also benefitting them as participants.

The principle underlying our filing test is that, if such a tied fare or rate is available on equal terms for sale by all willing participant carriers, there can then be no doubt that it is economically independent of the international travel to which it is tied for marketing purposes. Put another way, the fare must stand on its own, competitively and economically, as a domestic fare. Its level will be set independently, in response to domestic costs and competitive circumstances. A carrier simply will not price such a fare below its cost, because it has no interest in subsidizing the services of other carriers. Without the ability to restrict participation in the international travel to particular carriers, the offering carrier will have no leverage to require that profits from the international travel subsidize its domestic service. And without a carrier restriction, its fares *prima facie* will be competitively evenhanded in international service. The essential economic and competitive independence of such fares constitutes a substantive, rather than a formal, distinction from traditionally filed through (on-line and joint) fares. The distinction is

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[43] Indeed, present VUSA fares are even more sophisticated. As noted at the outset, they contain a number of restrictions which make such fares unattractive to the typical foreign business traveller as well.

[44] Current VUSA fares are all capacity-controlled and contain other restrictions which, in the aggregate, make it appropriate to evaluate the economics of such services on a marginal cost basis. In 1968 the Board was evaluating the economics of the Discount VUSA fares on a fully allocated cost basis.

consistent with the balancing of competing foreign and U.S. regulatory interests advocated as an explicit standard by BA. Such fares may still have some "international impact," but the interest of foreign governments in regulating them through the tariff mechanism is no greater than their interest in regulating combinable domestic U.S. fares. As we emphasized in ER-1246, that interest is insufficient to outweigh the U.S. interest in their regulation or, in this case, deregulation. They are essentially "domestic" fares from a factual, legal and policy standpoint.[45]

On the other hand, the carrier restriction raises the possibility that the tied fare is not economically or competitively independent. While the ALJ correctly found on this record that (1) there is no evidence of below-cost VUSA pricing or cross-subsidy from international services, and (2) the foreign carriers are not denied a fair opportunity to compete because of the presence of viable competitive alternatives, we nevertheless conclude that it is not unreasonable to subject such fares to bilateral tariff procedures. As BA points out, the restricted VUSA fares at issue may not be unfair competition within the meaning of the bilaterals, but they may still be international price

[45]The ALJ gave insufficient weight to economic and competitive forces in rejecting Northwest's basic contention that the Contract rate was its method of competing for domestic cargo revenues. He apparently assumed that the focus of rate must be international on the basis of Northwest's concession that the rate was a competitive response to a change in the commission structure of several foreign air carriers, not domestic competitors. Northwest's point, however, was that the higher commissions were reducing its domestic traffic and revenues between Chicago and Seattle by diverting such traffic over the Los Angeles gateway. Admittedly, the traffic in question was ultimately destined for the Orient, but that does not establish that the primary justification for the export restriction was the maximization of international service revenues or that its primary competitive impact would be on other international carriers.

competition in various important respects. We agree that there is a point on the spectrum where a mutual governmental interest in filing and review should be recognized, even though the precise degree of economic independence of a purportedly domestic fare may be uncertain or debatable.

We emphasize that there is nothing inherently "wrong" with any carrier-restricted VUSA fares. The fact that they cannot be presumed to be essentially independent domestic fares, and hence are made subject to formal scrutiny by the governments involved, does not suggest, either explicitly or implicitly, that they are economically unsound or competitively unfair in any respect. If such fares are challenged, when filed, their merits will be subject to discussion and negotiation as in the case of any other filed fares.

Viewed from this broader perspective, the distinction for filing purposes between carrier-restricted and other VUSA fares fully implements our mandate under the ADA, while not neglecting the bilateral context of section 403. It is consistent with the Board's policies and practices in the international pricing area.[46] Moreover, contrary to the assertion of BIA, DOT and the U.S. carriers, the distinction is not a wholly novel one for definitional purposes.[47] Generally, the on-line or interline availability of a

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[46]While the parties have quoted extensively from the policy considerations set forth in section 102 of the Act in support of diverse positions, we conclude that of all possible decisional options in this case, the filing test we adopt appears to be the most consistent with all these various factors.

[47]In *Qantas Empire, Foreign Transfer Traffic Case*, 29 CAB 33 (1959); and *Sitmar Cruises, Inc.*, Order 75-8-88, the Board concluded that an international through journey, for stopover purposes, would exist only if the international and internal domestic segments were performed by the same international carrier.

fare or rate does not matter for tariff-filing purposes. It only becomes a material factor when, as here, a separately offered fare or rate for transportation between domestic points is available only in conjunction with the purchase of international transportation. If such a marketing tie exists, the fare or rate is nevertheless domestic for filing and review purposes under the Act and the bilaterals if it is equally available for sale by all carriers.

We should emphasize several points with regard to our filing test. First, a "carrier restriction" includes not only the pure on-line restriction, but also any listing of international carriers whose fare is a condition of eligibility, regardless of whether such a listing relates on its face to a distinction in the price of the tied fare or to outright availability. Unless a restriction is on-line only, it is often difficult to tell from the listed "eligible" carriers whether the fare is available on equal terms to all passengers and carriers or whether some are intentionally excluded. To avoid uncertainty and to minimize factual conflicts, the carriers offering such fares will have to file them if the international transportation contains any reference to specific carriers.[48] We note again, in this context, that most current unrestricted VUSA fares use nonspecific provisions.

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[48]Procedurally, carrier-restricted VUSA fares will be treated like international joint fares under the Board's tariff rules in Part 221. The theory underlying our test is that tied fares lacking a carrier restriction are essentially separate "end-on-end" fares, not joint fares, while tied fares with a carrier restriction are essentially like joint fares in the economic, if not formal, sense. Carriers normally filing such fares will be responsible for filing the VUSA fares (listing all "participating carriers") with the Board and affected foreign governments. In the case of VUSA carriers not offering on-line service in a particular market, the filing carrier will be the international carrier and the VUSA carrier will be the participant.

A second point is that "equal availability" is only a filing criterion to insure that the tied fares and rates are fully distinguishable from international through fares, particularly joint fares. Treating carrier-restricted VUSA fares as if they were joint fares for filing purposes will not affect our treatment of the latter in any manner. In particular, carriers will not be restricted in their traditional ability to negotiate joint fare prorate agreements among themselves for filed international fares. Similarly, the Board's legal and policy options for resolving controversies in the international through fare area will not change. The intent and effect of our decision here is simply that to retain the status of a fare or rate tied to international travel as domestic for tariff filing purposes, a carrier will not be able to distinguish among carriers in terms of fare charged the passenger or the amount remitted.

The third point is that restrictions on tied fares other than overt carrier restrictions, such as travel on particular international fares or classes of service, or in particular markets, or even to/from particular airports, will not render such fares fileable, even though such restrictions in theory could be the subject of a complaint on fair opportunity to compete grounds. There are usually sound domestic reasons for restricting tied fares to particular markets or gateways, as evidenced by the presence of many such restrictions in "unrestricted" VUSA fares. Each carrier's domestic system strengths and needs will differ. There is no significant foreign regulatory interest in the filing of gateway-restricted tied fares and rates because competition will tend to make comparable programs available at the other gateways. JAL has in fact argued that, while Northwest's Contract rate was technically available to the international traffic of any carrier, it was carrier-restricted in a practical sense because, during the Contract period,

Northwest had the only regular freighter service to the Orient out of Seattle.[49] As noted by the ALJ, BIA and U.S carriers, however, JAL was able to match the constructed Chicago-Orient rate produced by Northwest's Contract Rate over its Los Angeles gateway, and there is evidence that the various export-restricted rates of U.S. carriers were competitively related.

Under our decision here, an unfiled VUSA fare or export rate restricted to a particular gateway, such as Seattle or Boston, should be unobjectionable to foreign carriers and governments for two reasons. First, since any foreign or U.S. carrier serving the gateway could participate in the VUSA fare on equal terms, the VUSA carrier could not afford to offer it unless it were profitable as a domestic fare. The foreign carrier concerns about below-cost pricing and cross-subsidization simply would not apply. And second, to the extent that the fare were successful in attracting foreign-originating or foreign-destined traffic over that particular gateway, U.S. carriers would be compelled to offer a similar fare or rate to their own gateway, and that fare or rate would have to be available without carrier restriction to remain unfilled. Thus, both domestic and international competition among U.S. carriers will tend to spread the benefits of attractive VUSAs to all international carriers. BA offers another illustration of this effect in describing Pan Am's reduction in its VUSA fare available to London-Washington, D.C. and London-Houston flights because it viewed those flights as competing with TWA's London-Philadelphia and London-New York flights which were eligible for a low TWA VUSA fare.

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[49] JAL has served the Seattle gateway since April 1, 1983, as a coterminal point with Chicago.

VI. The Bilateral Right to Compete Issue

The ALJ concluded that the VUSA fares and the Contract Rate at issue are consistent with the provisions in the U.S.-Japan, U.S.-Germany and U.S.-U.K. bilaterals which guarantee to the carriers of the signatory parties a fair opportunity to compete in providing the agreed services.[50]

First, he rejected the contention of JAL and Lufthansa that, given the cabotage restriction in the Act (section 1108(b)), their bilateral right to compete for traffic bound for interior U.S. points is violated as a matter of law to the extent that they are precluded from offering any VUSA fare to their passengers on terms equal to those offered to the international passengers of the issuing carrier, regardless of the availability and terms of interline VUSA programs of other U.S. carriers. He found such an "extreme" interpretation of the bilaterals to be without legal or factual support and inconsistent with the posture of their respective governments. And second, he rejected, as inconsistent with the record, the position of JAL and Lufthansa that the unrestricted VUSA programs of U.S. carriers do not provide acceptable competitive opportunities under the bilaterals because they are not comparable to the carrier-restricted programs at issue in terms of services (points, routings and schedules) or in terms of price. He found, *inter alia,* that the unrestricted VUSA programs

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[50]As noted by the ALJ, Article 8 of the 1955 U.S.-Germany bilateral, Article 10, of the U.S.-Japan bilateral, and Article 11(1) of the U.S.-U.K. bilateral provide for a "fair and equal opportunity . . . to operate" the agreed routes and services, while Article 5 of the 1978 Protocol to the U.S.-Germany bilateral provides for a "fair opportunity . . . to compete" in the agreed international services. He observed that no party drew any distinction between the two types of language, and neither did he.

are in fact functionally comparable and commercially competitive, that Lufthansa has captured a major share of VUSA traffic in its markets using such programs, and that any price disadvantage suffered by the complainants is of their own making because they have not attempted to negotiate prorate agreements to equalize the price for their passengers.

The ALJ's findings and conclusions on this issue are sound as a matter of fact, law and policy, and we affirm them consistent with our discussion herein. JAL and Lufthansa, the only parties challenging this aspect of his decision,[51] largely repeat their previous arguments, with little additional factual or legal support. However, given the central importance attributed to this issue in the original complaints, and the fact of its consideration on a full hearing record, we will address their arguments on review.

JAL and Lufthansa continue to advance the purely legal argument that, because the cabotage restriction denies them the ability to provide service between U.S. points, they are prohibited by law from providing "comparable" service and thus are legally denied a fair and equal opportunity to compete under the bilaterals. On review they also emphasize that their ability to compete for VUSA traffic whose needs are met by the unrestricted VUSA programs of U.S. carriers does not legally compensate for their inability to compete for VUSA traffic whose needs can only, or best, be met by the restricted VUSA programs. Similarly, they contend that an interpretation of the bilaterals which might require them to absorb some or all of a

[51] JAL has not argued on brief that the Contract rate denied it a fair opportunity to compete under the U.S.-Japan bilateral. The ALJ nevertheless addressed the issue and found that the record conclusively demonstrates that the rate resulted in no such denial. We agree with his findings.

VUSA price differential through a prorate or other agreement with the issuing carrier would impose an "unfair fee" on foreign carriers just to match restricted fares of U.S. carriers.

In effect, they argue that an on-line or similar carrier restriction is a *per se* violation of the bilateral right to compete provisions. We do not agree. As the ALJ found, the carriers have provided neither factual nor legal support for such an interpretation, and it is expressly at odds with the position of British Airways in this proceeding.[52] Moreover, as DOT emphasizes, the argument goes much too far. It assumes that the cabotage principle, reflected in Article 7 of the Chicago Convention and generally restated in our bilaterals, carries with it an implied obligation on the part of all carriers not to restrict the availability of any fare, domestic or international, to the issuing carrier or to selected participants.

The reasonable interpretation, implicitly adopted by the ALJ and articulated by BIA, is that the interests of the other signatory party's carrier must be taken into account so as not to unduly affect its economic opportunity to offer services covered by the agreement.[53] A "fair and equal"

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[52]He noted BA's acknowledgement that the VUSA fares at issue are not unlawful *per se* under the Act or the bilaterals, and its further explanation that, in the absence of significant market power in the relevant market or collusion by U.S. carriers against participation by foreign carriers, "it may be assumed that there are adequate competitive alternatives to the restricted VUSA fares." He found no evidence that the four U.S. carrier parties possess such significant market power and no evidence of any conspiracy to exclude foreign carriers. On the contrary, he found that the foreign carriers control a larger share of the traffic in transocean service than any single U.S. carrier. (BIA-IR-3; III TR 7.)

[53]BIA cites Article II (Japan), Article 11(2) (Bermuda II), and Article 5(b) of the German Protocol.

opportunity does not mean an identical opportunity, nor does it exempt carriers from normal commercial practices and the consequences of open price competition. In essence, what is required is that foreign carriers have the opportunity to offer reasonably competitive alternatives to particular internal point fares. The issue is therefore primarily a factual one, and there is no simple formula for determining a violation of these bilateral provisions.

The Board has been consistent in applying these principles. As BIA notes, in two recent Board orders (83-7-33 and 82-6-156) the Board rejected Qantas' contention that it was denied a fair opportunity to compete against Continental's "Koala" fare and $90 system arbitrary because it did not have direct access to the U.S. domestic points that Continental does and could only match Continental by "absorbing heavy prorate losses." The Board found that Qantas had numerous reasonable competitive alternatives to Continental's fares, including the ability to establish joint fares with other U.S. carriers, combine international fares with U.S. domestic fares, match the fares by reducing its arbitraries, and using other carriers' VUSA fares.[54] The Board expressly held that a reasonable opportunity is not denied because a prorate must be paid to U.S. carriers. Each carrier must decide for itself how it must compete, just as U.S. carriers must contend with the practical advantages of route structure and market identity that foreign carriers have within their own countries.

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[54]The Board also noted that Qantas itself offered on-line restricted excursion fares ("Circle 8", "Circle 4"), providing extensive travel opportunities over its South Pacific route system, including travel to various Australian and New Zealand points which Continental cannot serve, and that these had been approved by the Board. These were concededly international fares, filed in tariffs with the Board and with the Australian authorities.

JAL and Lufthansa contend that, on several occasions, notably *TWA* v. *Lufthansa* and *Air India Fares,* the Board has asserted the right to protect U.S. carriers from "analogous, but far less egregious, competitive handicaps" imposed abroad.[55] We disagree on both counts. In both cases, the Board expressly found that the disapprovals significantly restricted the practical, if not the legal, ability of U.S. carriers to compete for the international traffic in question. In contrast, the record here strongly supports the conclusion that there are no such significant restrictions on the ability of foreign carriers to compete for VUSA traffic in their respective markets. Significantly, both *Lufthansa* and *Air India* involved governmental action restricting the right of carriers voluntarily to match on-line through fares with interline through fares, not the right of individual carriers to deal with other carriers. Indeed, in *Air India,* the Board specifically endorsed the ability of Air India to offer restrictive on-line fares so long as competitors were not precluded from matching them among themselves on a voluntary interline basis.[56] The fact

[55]In *TWA* v. *Lufthansa,* (Order 81-2-68) the Board found that the German Government's refusal to permit TWA to match, through interline connections, certain Lufthansa through fares from interior German points, offered only on Lufthansa single-plane services, constituted "unjustifiable or unreasonably discriminatory restrictions on access of a U.S. carrier to a foreign market" under section 2 of the International Fair Competitive Practices Act, and it invoked sanctions under that statute. In *Air India Fares,* (Orders 81-7-160 and 81-10-67) the Board suspended certain Air India fares for service between the U.S. and India because the government of India prevented TWA from offering matching fares on an interline basis with all willing carriers serving the market.

[56]The Board's approach in resolving fair opportunity to compete complaints is also consistent with the conditions which it imposes on IATA agreements restricting fare combinability and other forms of competitive price matching. E.g., Order 78-67-113 (*Europe-Israel Fare Case),* and Orders 82-2-128, 82-4-10 and 82-9-1.

that here JAL and Lufthansa would prefer not to compete on a normal price basis is not a justification for Board intervention where equivalent competitive opportunities are available.

As we suggested at the outset of this investigation, the question is whether there are economically and commercially viable alternatives to restricted VUSA fares which are available to the passengers of the foreign carriers and which offer them a fair opportunity to compete for VUSA traffic in their markets. The ALJ correctly concluded that the unrestricted VUSA fares offered by numerous U.S. carriers do in fact provide reasonable alternatives and thus satisfy the bilateral provisions.

The ALJ first found that JAL and Lufthansa have participated in Pan Am's unlimited mileage VUSA fares since February 1981 (PA-1R-1); that their passengers pay the same VUSA fare level as Pan Am's own passengers (PA-R-2 and R-3); and that JAL and Lufthansa suffer no prorate dilution (II TR 122; PA-1R-3; PA-R-3 and 4). He then found that JAL and Lufthansa also participate in the systemwide unlimited mileage VUSA fares of American, Delta, Eastern and United, and concluded that "the evidence of record demonstrates that these U.S. carriers do provide a reasonably available, practical alternative" to the VUSA fares at issue.

With respect to the service comparability of the unrestricted fares, the ALJ found, first, that American, Delta, Eastern and United serve the great majority of cities that VUSA travelers on Northwest, Pan Am or TWA actually visit (TW-D-2 through 7; NW-8; FAC-SR-1, at 4); that each of these four carriers serves more U.S. cities than either Northwest, Pan Am or TWA (TW-D-2 through 7; NW-8; FAC-SR-1 at 4); and that Republic and Continental also have systemwide VUSA fares that serve the great

majority of cities VUSA passengers desire to visit (PA-12; NW-10).

Second, he found that competition among U.S. carriers at the leading cities was intense; that of the 12 cities that account for 70 percent of TWA's VUSA boardings (TW-1R-2), Eastern and American serve all 12 (TW-D-8), Delta and United serve all but St. Louis (used more as a "hub" than as a destination by VUSA travelers), and Republic serves all but Pittsburgh; that of the 8 cities accounting for 73 percent of Northwest's VUSA stopovers (NW-1; BIA-R-3 and 4), United serves all 8, while American, Continental, Delta, Eastern and Republic serve all but Honolulu (BIA-R-5); that of the 9 cities accounting for 69 percent of Pan Am's VUSA stopovers (BIA-R-6; NW-R-1), American, Delta, Eastern, Republic and United serve all 9; and that the conclusion remains the same if an analysis of single-plane or on-line service is made for the principle segments served by Pan Am (PA-11; BIA-R-7; I.D. at 48).

Third, he found that a comparison of the number of Lufthansa VUSA passengers who purchased domestic carrier VUSA fares to the total number of VUSA passengers carried by Capitol, Northwest, Pan Am and TWA conclusively demonstrates the viability of the former as commercial alternatives;[57] that for the period July 1, 1980 through June 30, 1981, Lufthansa carried 4,300 passengers on American's VUSA fare, 1,200 on Eastern's

[57]The ALJ noted that there is no record data on the usage of VUSA fares in the U.S.-U.K. market, and only U.S. carrier data for the U.S.-Japan market. He correctly concluded that, since JAL failed to provide the requested data, it must accept the conclusions that can be drawn from the evidence supplied by the other carriers. (I.D. at 48, n. 36.)

and 3,300 on United's for a total of 8,800 (FAC-18-3),[58] while Northwest carried 182 passengers between the U.S. and Germany (NW-1R-5 at 1); Capitol carried 273 (CA-1R-1); TWA carried 8,407, and Pan Am carried 4,795 (PA-R-9); that through the use of domestic carrier VUSA fares, Lufthansa has carried more U.S.-Germany VUSA passengers than any single U.S.-carrier; and that it carried almost as many on American's fare as Pan Am carried on its own restricted and unrestricted VUSA fares.

Fourth, the ALJ examined the service provided by the domestic carriers offering VUSA fares in the cities cited by JAL and Lufthansa in their sample VUSA itineraries [59] purporting to show that unrestricted VUSA fares involved more circuitous, less convenient travel than restricted VUSA fares. He found that all of the listed cities in FAC-T-1 and FAC-8 are served by at least one of the four U.S. domestic carriers that interline with JAL and Lufthansa, and most are served by more than one. In addition, he found that Pan Am's hypothetical itinerary in FAC-T-(LH) could be duplicated on any of the four, American, Eastern, Delta or United, while that for Northwest could be duplicated on either Eastern or Republic, and the hypothetical itinerary for Northwest in FAC-T-2(JL) could be duplicated on either United or

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[58] In addition, he noted, Lufthansa carried 1,304 passengers on Pan Am's unrestricted VUSA fare, for a total of 10,104 passengers in the U.S.-Germany market.

[59] These, he noted, were hypothetical itineraries based on Lufthansa's VUSA passengers traveling on American, Eastern and United (I TR 122-126).

Western.[60] He rejected any claim by the foreign carriers that only nonstop or direct service over the exact routings served by carriers offering restricted VUSA fares count as viable alternatives, finding that VUSA passengers actually use indirect, circuitous routings that often involve multiple connnections or backhauls, and travel via hubs such as Minneapolis and St. Louis to visit preferred cities and also noting that the foreign carriers themselves argue that VUSA passengers will endure circuitous routings and repeated transfers over any carrier to save money (I TR 210; FAC-1).

Finally, the ALJ addressed the contentions of JAL and Lufthansa that the unrestricted VUSA fares are not competitive alternatives because they would cost their passengers approximately $76 more ($250 more in the case of Honolulu commencements under the Northwest or Pan Am pass), an allegedly significant price advantage evidenced by the foothold gained by Capitol in the New York-Zurich market with a fare differential of $85 under Swissair's fare (FAC-SR-1 at 6; FAC-SR-13; FAC-R-5 and 6). He concluded that these price differentials do not place the foreign carriers at a competitive disadvantage, noting that Capitol's $85 advantage gained it a *de minimis* share of the New York-Zurich market in 1981 (BIA-1R-1 at 2) and finding "conclusive" proof in the fact that Lufthansa carried more VUSA passengers under the higher-priced fares in the U.S.-Germany market than any of the U.S. international carriers carried under their own fares.

[60] I.D. at 49. BIA further disputes the "assumption that routings over other city-pairs necessarily are more circuitous or involve more mileage," noting that a routing over United to visit the same points listed in the first Northwest itinerary in NW-IR-2 would involve one less segment and 74 fewer miles than if travel were on Northwest (FAC-SR-7).

He also agreed with BIA and the U.S. carriers, that foreign carriers also have the competitive alternative of being able to negotiate agreements with U.S. carriers under which they would pay part or all of the differential as a prorate.[61] He found that prorate agreements are a standard industry practice, and that the record does not indicate that JAL or Lufthansa have made any attempt to work out any sort of interline fare agreement with the carriers offering restricted VUSA fares (NW-1R-1 at 3). He concluded that they are asking for the Board to intervene in the marketplace to give them an advantage that other foreign carriers do not have, and that the obligations of the U.S. under the fair opportunity to compete provisions of the bilaterals do not compel such action.

JAL and Lufthansa's only rebuttal to this analysis consists of (1) the claim that the record contains no data on the number of Northwest, TWA, Pan Am and Capitol transocean passengers who purchased the VUSA fares of other U.S. carriers, and thus provides no basis for comparing the market share of foreign and U.S. carriers as the ALJ has done; (2) the citation of a TWA internal memo and other carrier testimony for the proposition that the

[61]NW-10. On review, BA also expressly agrees that, absent market power or collusion among U.S. carriers, a foreign carrier will probably be able to make alternative arrangements with another U.S. carrier through a prorate agreement to meet the competition of a restricted VUSA fare. It states that this is "fair" competition within the meaning of the bilaterals, but emphasizes that it is also essentially international price competition. It also observes that a particular restricted VUSA fare might be so discounted and require such an "exorbitant" prorate from a foreign carrier to subsidize a competitive response as to be unreasonable under the tariff requirments of the Act or the bilateral agreements. Our decision to subject restricted VUSA fares to international tariff procedures is not to be construed as a concurrence with this observation, which raises separate questions of economic analysis and regulatory policy.

primary purpose of the restricted VUSA fares was to give the issuing carriers an unmatchable competitive advantage in international markets; (3) the argument that the ALJ, BIA, DOT and the U.S. carriers confirm the existence of separate restricted and unrestricted VUSA program traffic markets by their suggestion that foreign carriers may negotiate prorate agreements to gain direct access to restricted VUSA programs for their passengers; and (4) the claim that accepting prorate absorption to gain competitive access to restricted VUSA programs or to match their lower price does not constitute fair opportunity to compete because some carriers, such as Lufthansa, are precluded as a matter of domestic law from entering into such prorate agreements.

None of these is persuasive. The possibility that the four U.S. carrier parties may have carried a number of undisclosed VUSA passengers on their transocean segments does not invalidate the ALJ's conclusions. The foreign carriers did not request such data. Our decision must be based on the record which they participated in developing. Moreover, it is not logical to assume that the number of such passengers would be large, given the evidence of the relative fungibility of VUSA programs. Most importantly, the ALJ's conclusions do not depend on a precise determination of Lufthansa's relative market share of VUSA passengers. The fact that Lufthansa carried a major share of VUSA traffic using unrestricted programs is not controverted and is clearly sufficient to establish the relative commercial and competitive viability of unrestricted VUSA fare alternatives for bilateral purposes.

As BIA notes, the citation of the TWA memo (TW-IR-4) or other U.S. carrier testimony adds little to the foreign carriers' case. Whatever the hopes of certain U.S.

carriers may have been in 1979, it is clear that by 1981 they recognized that any significant competitive advantage resulting from the introduction of a restricted VUSA fare was quickly lost because of the widespread and effective availability of unrestricted VUSA fares. TWA's observation is in full accord with the ALJ's extensive findings. There is no evidence of any structural impediment in the U.S. marketplace to effective competition by foreign carriers for all VUSA traffic.

The argument that there are really two VUSA markets, one for unrestricted VUSA fares and one for restricted VUSA fares, and that competitive parity in the former does not make up for disadvantage in the latter, is contrary to the ALJ's extensive findings on the service comparability of the various programs. There is no evidence that foreign carriers cannot compete effectively for all VUSA traffic. Indeed, they have done so even without attempting to gain access to every VUSA program or to match the precise level of every VUSA fare. The ALJ's recognition of the prorate option was not an acknowledgement of separate markets, but rather was a valid element in the analysis of what constitutes competitive fairness under the bilaterals.

The argument that restricted VUSA fares cannot be matched by some foreign carriers because prorate absorption is not permitted by their domestic law rests solely on the unsubstantiated opinion of a Lufthansa witness referencing a German law that appears analagous to the requirement of adherence to filed tariffs contained in section 403(b) of the Act. (1 TR 159.) His opinion is inconsistent with evidence that prorate arrangements to gain access to interline fares exist in Germany (1 TR 156-160) and that both Lufthansa and JAL have entered into such arrangements in the past (Orders 78-8-193 and 82-1-85).

Prorate-type arrangements are a common, if not a "standard" industry practice, and may properly be taken into account in considering the bilateral right to compete.

Finally, JAL and Lufthansa also contend that U.S. carriers use restricted VUSA fares to undercut the through fare between foreign and interior U.S. points in a way that foreign carriers cannot match. There is no evidence, cited or otherwise, that U.S. carriers promote VUSA fares in this manner or that a significant number of passengers use VUSA fares to undercut through fares, even though it is entirely permissible and often the case for through fares to be undercut by double ticketing or by tariff construction rules which incorporate domestic fares.[62] The combination of two or more fares to undercut a published through fare is not a rebate or otherwise unlawful under U.S. law. Nor does it contravene the bilaterals. See, *e.g.* Orders 72-10-1, 77-11-124, and ER-1246. Our decision on the tariff-filing issue herein does not alter this principle or its application to the fares and rate at issue.

VII. The Discrimination Issue

The instituting order asked whether the fares and rate at issue are unjustly discriminatory within the meaning of Sections 404(b) and 1002 of the Act.[63] The order also noted

[62]Northwest notes, for example, that its international tariffs filed with, and approved by Japan, Germany, and other countries, specifically provide that any U.S. domestic fare can be used to construct an international fare. CAB No. 55, Rule 8 (D) (13).

[63]Sections 404(b) and 1002 proscribe unust discrimination or undue preference or prejudice against "any particular person, port, locality or description of traffic." These are the traditional protections for the users of air transportation. Our discussion here is not directed to the concept or scope of discrimination against U.S. carriers embodied in section 1159(b) of the Act (section 2(b)(1) of the International Air Transportation Fair Competitive Practices Act of 1974). In view of

that the Board had recently liberalized its policy on price discrimination, including "status fares," (14 CFR 399.36, adopted by PS-93, June 27, 1980) and requested that evidence be developed so that findings concerning the fares and rate could be made on each of the elements set forth in that policy.[64]

JAL and Lufthansa argue that the VUSA fares unjustly discriminate (1) against the issuing carrier's non-VUSA passengers and in favor of its VUSA passengers by refunding to the latter a portion of their transocean fare in the

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this and our decision on the tariff-filing issue, we need not pass on the merits of the ALJ's finding that the U.S. carriers have not proved that they are subject to discriminatory practices abroad.

[64]Section 399.36 provides, in relevant part:

> (b) Except in unusual circumstances or as provided in paragraph (c) of this section, the Board will find a rate for domestic air transportation to constitute unreasonable discrimination only if:
>
> (1) There is a reasonable probability that the rate will result in significant long-run economic injury to passengers or shippers;
>
> (2) The rate is in fact discriminatory according to a reasonable cost allocation or other rational basis;
>
> (3) The rate does not provide transportation or other statutorily recognized benefits that justify the discrimination; and
>
> (4) Actual and potential competitive forces cannot reliably be expected to eliminate the undesirable effects of the discrimination within a reasonable period.
>
> (c) A rate that discriminates on the basis of the status of the traffic carried will not be presumed to be unreasonably discriminatory, unless the use of the status categories in question is contrary to established national anti-discrimination policy.

form of a below-cost VUSA program,[65] and (2) against foreign carrier passengers based on their "status" as prior and subsequent passengers on those carriers. They have also argued that the Board's policy statement in section 399.36 is limited to domestic transportation and, as such, is not applicable to the issues raised in this proceeding.

The ALJ concluded that the VUSA fares and the contract rate at issue are not unjustly discriminatory. He found, first, that PS-93 is applicable to the merits of the discrimination complaint on legal grounds, that carrier-restricted VUSA fares do not create a "status" discrimination as that term is used in PS-93, and that the record permits no affirmative findings that any of the elements required for a determination of unjust discrimination under PS-93 can be made. In particular, he found that there is no showing that the VUSA fares or the Contract rate are below cost, while the record conclusively demonstrates that competitive market forces tend to eliminate any injurious effects of the restrictions within a reasonable time. He also found that, even under pre-deregulation case law, a deviation from costs or a traceable rebate was a prerequisite to a finding of discrimination, and that no such rebate is demonstrated by this record. In addition, he found that discounts on one carrier do not, by themselves, discriminate against the traffic of another carrier under traditional case law. Finally, he found that the IATA agreement cases cited by foreign carriers are not relevant to the competitive fare and rate offerings in this case.

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[65]They similarly argue that the Contract rate unjustly discriminated against Northwest's Chicago-Seattle shippers and in favor of its Chicago-Orient shippers by rebating a portion of the published transpacific rate in the form of a lower "domestic" rate. They also argue that by using the Contract rate to construct a lower Chicago-Orient through rate, Northwest rebated a portion of the published Chicago-Orient through rate.

The ALJ's analysis is legally and factually sound. We affirm his findings and conclusions with several amplifications.

It is clear that the Board's Policy Statement in 14 CFR § 399.36 provides the framework within which the allegations of discrimination in the complaint should be assessed. The insistence of JAL and Lufthansa that the policy elements are not applicable, and in particular that they cannot be applied in a formal evidentiary proceeding without prior rulemaking procedures, is without foundation. See Order 82-7-70, *Pacific Common Fares Investigation.* In PS-93 itself, the Board emphasized that, with the adoption of IATCA, the statutory and policy framework for limited interference in carrier pricing decisions under section 404(b) was similar, if not identical, for international air transportation, but it decided, at least as an initial matter, to consider the applicability of the specific policy elements on a case-by-case basis because of the variety of competitive and regulatory circumstances in international markets. The Board expressly placed the policy and its elements at issue in this proceeding, and the foreign carriers have had a full opportunity to explore both their factual applicabiity and their consistency with bilateral understandings. They have done neither in this, the proper, forum. At the same time, the ALJ's findings on the elements themselves provide abundant support for the conclusion that regulatory intervention would be particularly inappropriate in this case. Whatever may be the competitive and regulatory environment between the gateways at issue in this proceeding, the record is clear that domestic competition may be relied upon to protect the interests of passengers to (or shippers from) interior U.S. points by insuring the availability of reasonable price and service options to the customers of every carrier.

JAL and Lufthansa rely completely on the continued applicability and vigor of pre-deregulation case law, contending that the Board's general policy statement cannot, in any event, overrule established judicial interpretations of section 404(b) of the Act. This ignores the altered statutory circumstances analysed by the Board in PS-93. We found, as a general legal proposition, that, with the adoption of the ADA and IATCA, competition is to be relied upon whenever possible to protect consumers, and the strict "rule of equality" which underlay many of the pre-deregulation discrimination cases is no longer of primary decisional significance. Where competitive market forces are reasonably free to operate, a more flexible view of differential pricing is to be encouraged. As discussed below, the cases relied upon by JAL and Lufthansa are distinguishable on their facts. However, their precedential value must also be weighed in light of a changing legal environment.

We agree with the ALJ, BIA and others that the record is inconsistent with a finding of unjust discrimination under either 14 CFR 399.36 or under pre-deregulation case law. First, the evidence precludes a finding that the challenged restrictions create "a reasonable probability . . . of a significant long-run economic injury" to passengers or shippers. Rather, it convincingly demonstrates that competition will tend to eliminate the undesirable effects of any discrimination within a reasonable period of time. Even under prior case law, section 404(b) is arguably satisfied because all passengers have the option of using the restricted VUSA programs of Northwest, TWA, Pan Am and Capitol, and all shippers had the option of using the export-restricted Contract rate if they met the volume

requirements.[66] However, the case against regulatory intervention based on economic discrimination becomes compelling given the fact that all passengers also have the option of flying a foreign carrier and using the unrestricted VUSA programs of U.S. carriers.[67] The unrestricted VUSA fares offer comparable services, and any price differentials are not significant enough to justify regulatory intervention. Indeed, they could occur only as a result of a business decision by foreign carriers not to incur any prorate dilution. In short, the alternatives to the restricted VUSA fares (and the Contract rate) are plentiful, and no prospective foreign carrier customer is without some reasonable VUSA (or export rate) option. It would be hard to argue that section 404(b) has ever required more.

Given the competitive alternatives available, the carrier and export restrictions are distinguishable from restrictions which the Board has disapproved in the past. In *Europe-Israel Fares*, for example, (Orders 78-7-113 and 79-2-130) the Board disapproved an IATA agreement imposing advertising, sales, combinability and passport/residency restrictions on U.S. passengers, fin-

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[66]*Pan American Ferry Flight Case,* 18 CAB 214 at 221, n. 9 (1953); *Delta Off-Peak Coach Fares*, 39 CAB 377 at 391 (1963). The foreign carriers do not challenge the foreign residency restrictions of the VUSA fares in this proceeding; and they do not challenge the volume restrictions of the Contract rate. The foreign residency restrictions were found not to constitute unjust discrimination under prior case law. *Discount USA Fares,* 48 CAB 892 (1968).

[67]Similarly, the Contract rate was open to all shippers, regardless of the means of transportation used beyond Seattle. Moreover, domestic competition prevented injury to shippers preferring other carriers or gateways, and eliminated the effects of any discrimination that may have existed. At least five other U.S. carriers offered competing export rates over other gateways, offering access to JAL and other foreign carriers (NW-IR-8).

ding that the agreement would deny them access to options that normal market forces would make available to others. No similar impairment of market choices is created by the fares and rate at issue.

A second basic conclusion from the record is that there is no evidence that the VUSA fares or the Contract rate are in fact discriminatory according to a reasonable cost allocation or other rational basis. As found by the ALJ, there is little or no direct evidence on costs, by carrier or by market. JAL and Lufthansa have at best presented only a computation of VUSA fare yields, showing that those of TWA, Pan Am and Northwest are below their system average yields (FAC-9; FAC-10). However, a showing of price or yield differentials alone does not indicate deviations from costs, and hence is insufficient to support a finding of discrimination under either pre-deregulation case law or under the Board's Policy Statement. The VUSA fares at issue are competitive offerings which encourage both domestic and transoceanic travel on the issuing carriers, filling empty seats and contributing to total revenues. There is no evidence that they are not economic on that basis.[68] Marginal cost pricing was recognized in PS-93 as an important and nondiscriminatory pricing technique.[69]

[68]Northwest notes that the foreign carriers have alleged that its VUSA yield is in the range of 5.23 cents/mile below its average system yield, but points out that yields in this range are not unusual for promotional fares used to fill empty seats. In 1982, for example, at least four other Northwest discount fares had similar yields (NW-IR-4).

[69]Similarly, the ALJ found no evidence that the Contract rate was uneconomic as a purely domestic rate. In fact, he found that the rate was at the same level as an existing domestic rate (1 TR 64-70-71) and was matched by at least one other U.S. carrier.

JAL and Lufthansa cite *Complaint of Hawaiian Airlines, Inc.* v. *Aloha Airlines, Inc.* Order 76-10-88, 71 CAB 868 (1976), affirmed *sub nom. Aloha Airlines, Inc.* v. *CAB,* 598 F.2d 250 (D.C. Cir. 1979), for the proposition that the restricted VUSA fares discriminate against U.S. carrier transoceanic passengers who do not want a VUSA program, and for the proposition that the Contract rate discriminated against Northwest Chicago-Seattle shippers who did not want connecting service to the Orient, on the theory that the marketing tie permitted a selective rebate of part of the transocean fare. The ALJ correctly distinguished *Aloha* on the facts, observing that the Court of Appeals sustained a Board finding that an arrangement between Aloha and Budget-Rent-A-Car, providing a 50 percent car rental discount to Aloha passengers, was an illegal rebate of the air fare and was unjustly discriminatory because, on the facts, Aloha's payments to Budget subsidized the rental discount itself, in addition to covering Aloha's share of the joint program's promotions costs. He found that JAL and Lufthansa merely claim that the $76 differential between an illustrative unrestricted VUSA fare at $475 and a restricted VUSA fare on TWA at $399 is a credit or rebate, and concluded that without evidence on costs, such a claim is baseless.

To the extent *Aloha* reflects a strict application of the rule of equality, it is no longer sound precedent. Moreover, the case is *sui generis* because it involved non-airline services. Fares or airline services open to all are traditionally not discriminatory against those not wishing to use them. We do not read *Aloha* as altering this basic principle.

JAL and Lufthansa also cite a number of cases, particularly *Interstate and Intrastate Fares in California and*

Texas Markets, Order 76-7-23, for the proposition that the restricted VUSA fares unlawfully discriminate among identically situated through passengers solely on the basis of the carrier selected for transportation over a prior sector of the journey. They contend that these cases are direct precedent because fare discrimination based on "status," need not meet the criteria spelled out in PS-93 for a finding of unjust discrimination, and that status includes such carrier selection. Several points should be emphasized. First, the ALJ observed that PS-93 defined "status" fares as those "based on such factors as age and status, not transportation-related factors such as cost savings" and he correctly found that the carrier used for a prior segment is clearly an economic or transportation-related factor.[70] Second, the Board's *Interstate and Intrastate Fares* decision does not support the proposition that the carrier restriction discriminates against the passengers of other carriers on the basis of their status. In that case the Board found that it was unjustly discriminatory for a carrier to charge its own passengers different fares for a given intrastate flight solely because some had an "interstate" itinerary disclosed on their ticket. Given the ease and frequency of double-ticketing, the Board found that such a dual fare structure unjustifiably distinguished between knowledgeable and unknowledgeable passengers receiving what was otherwise an identical service on the same carrier. The case is simply not on point, even if it were unquestionably good

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[70]Moreover, the Board's elimination of the traditional presumption that "status" fares are illegal under the rule of equality (letting stand the presumption against status fares that violate other statutory or constitutional antidiscrimination standards) was not intended to create a separate standard of evaluation of such fares under the Policy Statement. The policy statement applies equally to all forms of price discrimination among passengers, except to those based on "invidious" factors such as race or citizenship.

law and policy under the present statute. And third, as BIA and Northwest emphasize, the logic of the legal analysis proposed by JAL and Lufthansa is that discounts for on-line travel are *per se* unjustly discriminatory. Yet such restrictions are fairly common and most have never been challenged. In this context, BA concedes that it is not unjustly discriminatory *per se* for a U.S. carrier to seek to promote certain of its international services by tying them to VUSA fares on its domestic services.

Accordingly, pursuant to sections 403 and 204 of the Federal Aviation Act of 1958, as amended,

1. We find and conclude that: (1) the carrier-restricted VUSA fares at issue should be classified as international for filing and review purposes under the Act and the relevant bilaterals; (2) the export-restricted Contract rate is not international for filing and review purposes; (3) the fares and the rate at issue are not inconsistent with bilateral guarantees of a fair and equal opportunity to compete; and (4) the fares and the rate at issue are not unjustly discriminatory under sections 404(b) and 1002 of the Act;

2. We direct all air carriers and foreign air carriers to file tariffs with the Board and with foreign governments, consistent with bilateral obligations, within 30 days of the date of service of this order, setting forth the terms and conditions of all fares and rates for transportation between or among domestic (or foreign) points which are available only in conjunction with the purchase and use of air transportation to and/or from the United States on a specified carrier or carriers;

3. To the extent not granted herein, we deny all motions and other requests for relief in Docket 40269; and

4. We terminate this proceeding.

By the Civil Aeronautics Board:

PHYLLIS T. KAYLOR
Secretary

(SEAL)

All Members concurred.

APPENDIX C

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D.C.

VISIT USA FARE/EXPORT INLAND CONTRACT RATE INVESTIGATION

DOCKET 40269

INITIAL DECISION OF ADMINISTRATIVE LAW JUDGE JOHN M. VITTONE

*Served: June 3, 1983

Found that:

(1) the Visit USA fares and the Export Inland Contract rates at issue in this proceeding should be classified as international fares and rates under the Act and the civil air transport agreements;

(2) the Visit USA fares and Export Inland Contract rate at issue in this proceeding are not unjustly discriminatory within sections 404(b) and 1002 of the Act; and

(3) the Visit USA fares and Export Inland Contract rate at issue in this proceeding are consistent with the civil air transport agreements which guarantee a fair opportunity to compete.

*Service List attached as an Appendix

Petitions for discretionary review of this initial decision must be filed within 21 days after date of service in conformity with 14 C.F.R. §302.28 of the Board's Rules of Practice.

Appearances:

Laurence A. Short, Arthur D. Bernstein, David E. Short and *Suzette Matthews,* for Japan Air Lines, Co., Inc. and Lufthansa German Airlines.

William C. Clarke and *James D. Tussing,* for British Airways.

Lawrence D. Wasko, O.D. Ozment and *Kevin F. Meckus,* for Capitol International Airways, Inc.

Ronald D. Eastman, Barry S. Spector and *Lynda S. Mounts,* for Northwest Airlines, Inc.

David M. O'Connor and *John M. McCaffery,* for Pan American World Airways, Inc.

Robert W. Dillon and *George N. Kenyon, Jr.,* for Trans World Airlines, Inc.

Connie Reshard and *Ann Verber,* for the U.S. Department of Transportation.

William J. Wagner, for the Bureau of International Aviation.

TABLE OF CONTENTS

	Page
INTRODUCTION	1
VISIT USA FARES	3
The Foreign Carriers' Complaint	10
VUSA-Type Fares Offered by Foreign Carriers	13
INTERNATIONAL V. DOMESTIC	14
UNJUST DISCRIMINATION	28
The Board's Policy Statement - 14 C.F.R. 399.96	30
Discrimination Against the U.S. Carrier's non-VUSA Passengers	36
Discrimination Against Foreign Flag Carriers' VUSA Passengers	38
Miscellaneous	40
DO THE VUSA FARES DENY FOREIGN AIR CARRIERS A FAIR OPPORTUNITY TO COMPETE?	41
The Bilateral Agreements	41
Positions of the Parties	42
Discussion	44
DISCRIMINATION ABROAD AGAINST U.S. CARRIERS	52
EXPORT-INLAND CONTRACT RATE	52
International v. Domestic	53
Unjust Discrimination	57
Fair Opportunity to Compete Under the Bilateral Agreement	59
ULTIMATE FINDINGS AND CONCLUSIONS	59

RECOMMENDED DECISION OF ADMINISTRATIVE LAW JUDGE JOHN M. VITTONE

INTRODUCTION

By Order 81-11-182, December 1, 1981, the Civil Aeronautics Board instituted an investigation into the legality of the "Visit USA" (VUSA) fares of Northwest Airlines, Inc. (Northwest), Pan American World Airways, Inc. (Pan Am), and Trans World Airlines, Inc. (TWA), and of the Export Inland Contract Rates of Northwest. The investigation was instituted as a result of a complaint by Japan Air Lines Company, Ltd. (JAL) and Lufthansa German Airlines (Lufthansa) in Docket 38899 seeking the suspension and investigation of the Visit USA fares,[1] and a complaint by JAL in Docket 39595 against the Export Inland Contract Rates of Northwest. The VUSA fare of Capitol Air, Inc., was consolidated into this investigation by Order 82-2-30, February 5, 1982, after a complaint against the fare was filed by Lufthansa in Docket 40420. British Airways was granted leave to intervene at the hearing as a result of its complaints in Dockets 40861 and 40945 against revisions to the VUSA fares under investigation of TWA and Pan Am in certain United States-United Kingdom markets. (1 TR 10)

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[1]Philippine Airlines, Inc., Singapore Airlines, Limited, and Swissair, Swiss Air Transport Company, Ltd., joined in the complaint in Docket 38899. China Airlines, Ltd., filed a separate complaint in Docket 39028. These carriers have withdrawn from the investigation. ([sic] *See* Orders of the Administrative Law Judge, February 19, June 23 and August 2, 1982). The complaint in Docket 38899 also named the Visit USA fares of Western Air Lines, Inc., and Braniff Airways, Inc. The complaint against Western was dismissed by Order 81-11-182 at the request of the complainants. Braniff was dismissed as a party after it ceased operations and entered into reorganization proceedings under the Bankruptcy Code. (*See* Order of the Administrative Law Judge, May 28, 1982).

As set forth in the instituting order and reaffirmed in an Order on Reconsideration, Order 82-1-83, the primary issue of this investigation is whether the Visit USA fares of Capitol, Northwest, Pan Am and TWA, and the Export Inland Contract Rates of Northwest, are unlawful under the Federal Aviation Act of 1958, as amended, and the civil air transport agreements between the United States and the Federal Republic of Germany, Japan, and the United Kingdom.

The order of investigation established three specific subissues:[2]

(a) Are the Visit USA fares and the Export Inland Contract rates unjustly discriminatory within the meaning of sections 404(b) and 1002 of the Act;

(b) Should the Visit USA fares and the Export Inland Contract rates be classified as domestic or international fares or rates under the Act, and the various civil air transport agreements;

(c) Are the Visit USA fares or Export Inland Contract rates inconsistent with the provisions of the civil air transport agreements which guarantee a fair opportunity to compete.

Prehearing conferences were held on February 11, May 25, and August 2, 1983. Oral evidentiary hearings were held on September 14, 15, 16, 1982. Following the hearing, post-hearing exhibits were filed by Pan Am, TWA, and the Foreign Air Carriers. Opening briefs were filed on November 24, 1982 and reply briefs were filed on December 15, 1982.

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[2]Order 81-22-182 sets forth as a fourth subissue whether the Visit USA fares are in violation of section 1 of the Sherman Act. JAL and Lufthansa moved on June 17, 1982, to amend their complaint to withdraw the allegation of a section 1 violation. By Order dated July 8, 1982 of the Administrative Law Judge, this subissue was dismissed from the case.

VISIT USA FARES

Visit USA (VUSA) fares have been offered since about 1968 and numerous U.S. carriers currently offer this type of fare.[3] In general, these fares, which range in price from approximately $400 to $500, provide unlimited travel, subject to varying restrictions, over the domestic route systems of the U.S. carrier offering the fare for specified times ranging from 14 to 90 days. In some cases, Canada is included at no extra charge, but frequently a higher rate is charged if Honolulu, Canada, Alaska or Puerto Rico is included.[4]

All of the VUSA fares are subject to other restrictions on their use. Generally, they are capacity restricted and require that the fare be purchased and the itinerary booked outside the United States prior to the commencement of travel from abroad. In some cases, the VUSA fare may be purchased within the United States upon payment of a $100 surcharge. In most cases, changes in itinerary can be made for a service charge of $20-25. Although the VUSA fares provide for unlimited travel over a carrier's domestic system for a certain number of days, some carriers place a restriction on the maximum number of coupons that can be issued, and other carriers place restrictions on stopovers and connections at a particular city. Many carriers limit the number of transcontinental flights that can

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[3]FAC-IR-1. In addition to the carriers under investigation, the following carriers offer VUSA type fares: Delta, Eastern, Republic, Ozark, Continental, USAir, Western, Wien, United, American and Aloha. (PA-12).

[4]Pan Am offers a VUSA fare which allows the passenger to travel to and from points in Mexico, as well as between points in the U.S.; Northwest offers a VUSA fare which permits travel to and from Canada, as well as between points in the U.S. (PA-IR-1 at 5; Northwest IR-1 at 1) These fares are conceded by Pan Am and Northwest to be international fares and are filed with the Board in international tariffs. (*See* Pan Am Reply brief at 2-3, Northwest Reply Brief at 10).

be made. All carriers place a limit on the maximum travel period allowed or require that all travel be completed within a certain number of days of arrival in the United States. In addition, some carriers have prohibitions against, or blackout periods for, weekend or holiday travel.

The distinguishing characteristic of the system-wide VUSA fares of the four carriers that are under investigation from the system-wide VUSA fares of other U.S. carriers not under investigation is that the fares of TWA, Northwest, Pan Am, and Capitol are available only to foreign-originating passengers who use the foreign air transportation of the U.S. carrier offering the fare, or of other carriers specified in the tariffs, to travel to and from the United States.[5] In addition, the VUSA fares are avail-

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[5]The VUSA fares of all the U.S. carriers were published in ATP Tariff CAB No. 352. The specific tariff provisions under investigation are:

Capitol	Rule #1058, Visit the USA on CL.
Northwest	Rule #1022, Transatlantic U.S.A. Pass and Rule #1023, North/Central Pacific U.S.A. Pass.
Pan American	Rule #1030, Visit the U.S.A. on PA, and Rule #1035, South Pacific Visit the U.S.A. on PA.
TWA	Rule #1025, Domestic System Visit U.S.A Fares, and Rule #1051, Transpacific Visit U.S.A. Fares.

Even though TWA's transpacific VUSA fare has been put in issue in this proceeding, it is available to passengers travelling to and from the Untied States on the transpacific scheduled service of any international carrier. Pan Am point-to-point VUSA fares are not at issue in this proceeding (PA-IR-1).

The specific fares that BA complained against are the reduction by TWA of its VUSA fare to $296 in the London (Heathrow)-Philadelphia and London (Gatwick)-New York markets from July 11 until September 6, 1982, and the reduction by Pan Am of its VUSA

able only to non-U.S. residents or active duty U.S. military personnel stationed outside the United States. The VUSA fares are sold on separate ticket stock from the international ticket. (2 TR 95, 147, 148, 244)

In order to purchase unlimited mileage VUSA travel, the international passenger is required to show to the travel agent or airline ticket agent some proof of foreign residence, and his transoceanic ticket as proof of how he travelled to the U.S. (See TW-IR-3, p. 1; PA-IR-1, Attachment A; Northwest IR-3) In addition, reservations are usually made for the entire trip when the ticket is purchased. (2 TR 147, 148)

The VUSA passenger can purchase his VUSA ticket at the point of origin, or after his arrival in the U.S. For example, Northwest's VUSA tariffs effective July 23, and September 7, 1980 provide:

> A special booklet of 8 Flight Coupons will be issued to the passenger by a NW office either outside the U.S. prior to transatlantic travel or inside the U.S. after arrival. The coupons will be completed for desired travel as the passenger determines his travel plans . . . . In the event the passenger uses all 8 coupons and desires additional travel within the period of validity of the fare, he may obtain an additional book of flight coupons at no extra charge from any Northwest Airlines office within the United States. (Northwest IR-3 at 1)

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fare to $299 in the London (Heathrow)-Washington, D.C. and London (Gatwick) [sic]-Houston markets from August 12, 1982 until December 15, 1982. Orders 82-8-93 and 82-9-42 denied BA's complaints because these fares were simple revisions of fares that were already under investigation.

Pan Am's unlimited mileage VUSA tariff originally required that the VUSA transportation be purchased abroad at the passenger's point of origin. (PA-IR-1, Attachment A) On September 20, 1980, advance booking requirements were abolished, and Pan Am VUSA passengers are permitted to purchase their entire VUSA transportation in the U.S. (*Id.* at 2) TWA's unlimited mileage VUSA tariff, in effect since January 1, 1980, contained no restrictions with regard to place of purchase. However, several years ago TWA added a $100 surcharge to its VUSA fares purchased in the United States in order to encourage TWA passsengers to purchase their VUSA transportation at their point of origination. (TW-R-1)

The typical VUSA passenger uses an unbundled coach fare or a promotional fare such as an Apex or a Group Inclusive Tour fare to get to the United States (1 TR 155; 1 TR 95; 3 TR 42). These fares are generally used only to get to the U.S. gateway. Pan Am determined that 77 percent of its VUSA passengers who bought their unlimited mileage VUSA tickets abroad started and ended their trip on the fare at the same U.S. gateway. (PA-6). Fifty-nine percent of Pan Am's VUSA passengers started their trip at New York, while 61 percent ended their trip at New York. The comparable figures for Miami were 24 and 27 percent. Sixty-four percent of its VUSA passengers who were issued coupons in the United States started and ended their use of the VUSA fare at Miami, Detroit, New York or Houston. (PA-5).

The overwhelming majority of Pan Am, Northwest, and TWA VUSA travelers purchase their VUSA transportation abroad before departing for the United States. Northwest etimates that 80 percent of the Northwest VUSA travel is purchased abroad; Pan Am estimates that

96.1 percent of Pan Am VUSA travel is purchased abroad; TWA states that "virtually all" TWA VUSA travel is purchased abroad. The Capitol Air VUSA can only be purchased overseas before the passenger commences his travel to the U.S. (CL-IR-2) Thus, in the vast majority of cases the passenger planned his VUSA U.S. itinerary before he departed for the United States.

Northwest estimates that its VUSA passnengers travel on the average only 3.6 VUSA segments;[6] each segment is on the average 1,264 miles. (Northwest IR-1 at 1) Pan Am estimates that its VUSA passengers travel an average of 5.6 segments. (PA-IR-10; 2 TR at 109-110) TWA estimates that its VUSA passengers used on an average 7.7 flight coupons, with an average total VUSA mileage of 6,592 miles. (TW-IR-2, p. 1).

Lufthansa and JAL argue that the restricted VUSA fares of Pan Am, Northwest, TWA, and Capitol have a significant impact on their operations. (FAC Brief at 17-19) According to their calculations, in 1981 at least 10 percent of the passengers in the Germany-U.S. market used VUSA fares. This figure includes 10,104 passengers of Lufthansa who were able to purchase the VUSA fares of American Airlines, United Air Lines, Eastern Airlines, *and Pan Am*. Thus, according to its own figures, Lufthansa carried about 43 percent of the total traffic in the Germany-U.S. VUSA market, more than any other single U.S. carrier.

An important matter with respect to TWA's Germany-U.S. passenger data should be discussed at this point. At a late stage in this proceeding, TWA revised Exhibit TW-

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[6]However, for 22 sample itineraries on Northwest, the VUSA passenger traveled an average of 5.9 segments per itinerary. (NW-2)

IR-5 to change its estimate of the number of passengers in its FRA-JFK market that made use of its Unlimited Travel VUSA fare in 1981 from 8,407 to 3,422 passengers. (2 TR 152-156, 159-65) As a result of this change, its original estimate that this group constituted 9.6 percent of the roundtrip on-board passengers in the FRA-JFK market during 1981 was also reduced to 3.9 percent. The carrier claims that its overstatement was due to a "misinterpretation of the survey at an early stage of application." (TW-IR-5 Revised) The Foreign Air Carriers in surrebuttal exhibit FAC-SR-25 maintain that a simple application of the survey-indicated percentages of TWA Germany-U.S. VUSA passengers to the toal TWA Germany-U.S traffic is the approach that would yield the most accurate data.

TWA has simply failed to show why application of the survey findings to the population would not provide results that would be consistent with the known facts as the foreign carriers contend. TWA has stated that the survey period was chosen to avoid bias; that the derived 9.3 percent of on-board Frankfurt-New York passengers using VUSA fares during the survey period was "correctly established"; and that during the survey period it carried 87,678 on-board Frankfurt-New York passengers. A straight-forward application of 9.3 percent survey results in the U.S.-Germany markets to TWA's passenger figure of 87,678 would yield the result of 8,154, a number substantially closer to its original estimate.[7]

[7]In view of the fact that the difference between the results of TWA's original estimate, the foreign carriers' calculation, and the calculation performed above is insignificant, TWA's original estimate will be used throughout this decision.

In addition, there is also a question as to the propriety of one of TWA's other computations. On page 9 of TW-IR-5 (Rev.), column (d). TWA derived percent of total roundtrip on-board passengers us-

In the Japan-U.S. market, the foreign carriers argue that at least 6.2 percent of passengers used VUSA fares during calendar year 1981. The data available in the record is only for Northwest and Pan Am. JAL did not provide any data on the number of VUSA passengers it carried for connection with Pan Am's VUSA program or any other carrier's program.[8] JAL asserts that the "amount of traffic diversion represented a loss to JAL of approximately $10 million to $20 million in revenue." (FAC Brief at 18, 1 TR 170). There is no substantial basis in this record to support that allegation.[9]

While the foreign carriers argue that the VUSA traffic is significant, the Bureau and other parties argue that the amount of traffic represented by the VUSA passengers is *de minimis*. In their view, the amount of traffic represented by the VUSA passengers represent only 3.3 per-

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ing VUSA fares by dividing the data in column (b) by the data in column (c). However, the data do not appear to be comparable. Column (b) data refers to "individuals" while column (c) data refers to on-board passengers. Thus an individual is counted as one passenger in (b), but would be counted as two passengers in (c) on a roundtrip transatlantic flight. In order to make the data in both columns comparable, data in (b) would have to be doubled or those in (c) halved. The result would be a doubling of the data in column (d) and a doubling of the end result when brought to its logical conclusion.

[8]In the instituting order, the Board stated that it expected all parties to cooperate in the information gathering process. In this instance, JAL failed to cooperate.

[9]The only basis in the record for the figure is the testimony of JAL's witness, David Landyke. (1 TR 170) Mr. Landyke testified that the total revenue for all Japan-U.S. VUSA passengers would be $18-$20 million. JAL appears to assume that it would attract all of the VUSA traffic if Northwest's and Pan Am's programs were available to them without restrictions. The figure is meaningless. On reply brief at 57-58, JAL argues that this foreclosure from the market could eliminate the carrier's annual profit at some point. Again there is no basis, other than JAL's speculation, for this allegation.

cent of the Germany-U.S. market and 1.8 percent of the Japan-U.S. market. (BIA Brief at 34-35) The main difference between the parties on this point is that the foreign carriers argue that "gateway-to-gateway" traffic should be excluded from the calculation because only passengers who travel beyond the U.S. gateway are potential VUSA passengers. (FAC-R-10 (rev.) and R-11) There is some merit to this argument. However, in order to assess whether the VUSA fares have foreclosed the foreign carriers form a fair opportunity to compete under the bilateral agreements (discussed *infra.*), it will be necessary to assess how the VUSA fares fit into the total Germany-U.S. and Japan-U.S. markets.

Regardless of the characterization of volume of traffic, the VUSA fares amount to no more than 10 percent of the Germany-U.S. market, and Lufthansa carries a substantial amount of that traffic. In the Japan-U.S. market, VUSA traffic accounts for considerably less, and we do not know how much JAL accounted for in the market.

Finally, it should be noted that only TWA and Capitol exclude all other carriers from participating in their VUSA programs. Northwest permits four foreign carriers to sell the transpacific VUSA fares for passengers originating in the South Pacific subject to the same rules and conditions as Northwest. The four carriers are Qantas, Air New Zealand, CP Air, and UTA (Northwest IR-1 at 3). Pan American permits 34 foreign carriers to participate in its VUSA program, including JAL and Lufthansa (PA-IR-1, 3). Since February 20, 1981, Pan Am's unlimited VUSA program has been available to JAL and Lufthansa passengers on a connecting basis and at the same fare level as passengers who use Pan Am's transocean service. (PA-R-2, 3).[10]

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[10]Pan Am's VUSA fare via Honolulu is not available to JAL. (FAC R-5 (rev.)).

The Foreign Carriers' Complaint

As noted above, for many years, various U.S. carriers have offered VUSA fares which permit foreign residents to travel to numerous U.S. cities on an unlimited mileage basis for a fixed price. The specific fares which are at issue in this proceeding are the "restricted" VUSA fares implemented several years ago by Northwest, Pan Am, TWA, and Capitol. These carriers restrict the availability of their VUSA fares to those passengers using that same carrier's transoceanic services to fly to and from the United States.[11]

The Foreign Carriers complaint against these restricted VUSA fares is based on three arguments. First, because the fares apply to one portion of a continuous international movement, the restricted VUSA fares are in "foreign air transportation" as defined in section 101(24) of the Act (49 U.S.C. 1301). Therefore, the foreign carriers argue that they should have been submitted to the foreign governments involved (as required by applicable bilateral air transport agreements, section 1102 of the Act, and the U.S. air carriers' certificates), and should have been filed with the Board (as required by section 403 of the Act), as tariffs for foreign air transportaion. The U.S. carriers have not filed the VUSA fares with the Board or foreign governments.[12] Second, because the restricted VUSA fares cannot be sold to passengers using the foreign carriers' transoceanic services, or can only be sold to those passen-

[11]*See* Exhibits TW-IR-3 at 1; PA-IR-1, Attachment A; Northwest IR-3; CL-IR-2.

[12]There is no evidence that the governments of Japan or Germany have directed that the VUSA fares of the four carriers under investigation be filed with their respective aviation agencies. There is evidence that Delta Airlines has filed its VUSA with the German aviation authorities. (1 TR 151)

gers at a higher price, and because the foreign carriers are by law prohibited from themselves providing matching services in the U.S., these restricted fares deny the foreign carriers a fair and equal opportunity to compete in the Germany-U.S. and Japan-U.S. markets. Third, because the fares serve to refund a portion of the transoceanic fare to those pasengers purchasing a VUSA ticket, they discriminate against the U.S carriers' other transoceanic passengers who do not purchase a VUSA ticket. Further, the fares constitute a "status" discrimination against those passengers who travel on foreign-flag carriers to and from the U.S., denying them access to the VUSA program, or charging them more for their VUSA ticket, based solely on their status as foreign-flag transoceanic passengers.

There are two restrictions that the U.S. carriers attach to their VUSA fares, and to which the Foreign Air Carriers object.[13] First, some restricted VUSA carriers reserve their VUSA fares only for passengers using their transoceanic services to travel to the U.S. This "on-line" restriction excludes passengers travelling to the U.S. on a foreign carrier from purchasing VUSA travel on their system. With respect to residents of Japan and Germany, both Northwest's and TWA's unlimited mileage VUSA fares are of this type.[14] Pan Am's unlimited mileage VUSA is also

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[13]Some U.S. carriers offer unlimited mileage VUSA fares not restricted as to the transoceanic carrier. *See* Fn. 3, *supra*. and ATPCO Passenger Tariff Set, August 2, 1982. These unrestricted, unlimited mileage VUSA fares are not at issue in this proceeding. Some U.S. carriers also offer VUSA fares for travel between specific city-pairs in the United States ("point-to-point VUSA fares.") Except for Capitol Airways (CL-IR-3 and CL-A), these point-to-point VUSA fares are generally made available to any foreign resident regardless of what carrier he selects for the transoceanic haul, and are not at issue in this proceeding. (*See* 2 TR at 29)

[14]*See* Northwest IR-3, TW-IR-3.

restricted to Pan Am's transoceanic passengers. However, as noted above, numerous foreign carriers participate in the Pan Am unlimited mileage VUSA, including JAL and Lufthansa; so many that it may be argued that the restriction has been emasculated by the exceptions. Second, some VUSA carriers make their VUSA program available to transoceanic passengers of selected other carriers, but only at a higher price than that at which the program is made available to passengers also using the VUSA carrier for the transoceanic haul.[15]

VUSA-Type Fares Offered by Foreign Carriers

In its Order 81-11-182 at 8, the Board directed the U.S. carriers to "fully support with specific factual evidence their allegations . . . that foreign carriers offer their own versions of Visit U.S.A. fares over some or all of their internal domestic systems which are filed as domestic fares within the foreign country and are available only to international carriers from abroad when travel is over the foreign carrier." The evidence of record does not demonstrate that there are any VUSA-type fares offered by foreign carriers which are treated as domestic fares in their countries and are only available to passengers who travel on the foreign carrier.

In PA-1, Pan Am cited three VUSA-type fares offered in Brazil, France, and India.[16] Unlike the VUSA fares at issue, none of these fares contain a restriction against participation based upon the carrier the passenger used for the transoceanic travel. (2 TR 137) These fares are available at the same fares and times to all passengers regard-

[15]See PA-IR-3; PA-R-2, 3.

[16]See PA-1. The fares are the "TransBrazil Air Pass", "Visit France" fare, and "Discover India" program.

less of how they travelled to the foreign country. No party offered any evidence concerning any VUSA-type fares which may be offered in Germany or Japan and which may contain restrictions similar to the VUSA fares at issue.

INTERNATIONAL V. DOMESTIC

In Order 81-11-182, the Board required the detailed exploration of whether the VUSA fares should be classified as domestic or international fares under the Act and the various bilateral agreements. In this regard the parties were directed to provide comprehensive factual evidence as to whether the fares as actually applied are typically part of a continuous integrated international journey originating and terminating in a foreign country. (Order 81-11-82, at 8). At the hearing and on brief, the foreign air carriers (and British Airways) argued strongly that the restricted VUSA fares are in "foreign air transportation" as defined in section 101(24) of the Act and that the fares should have been submitted to the foreign governments involved as required by the bilateral agreements, section 1102 of the Act, and the U.S. carriers' certificates. Accordingly, the foreign carriers argue that the restricted VUSA fares should have been filed with the Board for foreign air transportation as required by section 403. The other parties disagree with contentions of the complainants.

Section 101(24)(a) defines "interstate air transportation" as:

> the carriage by aircraft of persons or property for compensation or hire, or the carriage of mail by aircraft, or the operation or navigation of aircraft in the conduct or furtherance of a business or vocation, in commerce between, . . . a place in

> any state . . . or the District of Columbia, and a place in any other state . . . or the District of Columbia . . . (49 U.S.C. §1301(24)(a))

Section 101(24)(c) defines "foreign air transportation" as:

> the carriage by aircraft of persons or property for compensation or hire, or the carriage of mail by aircraft, or the operation or navigation of aircraft in the conduct or furtherance of a business or vocation, in commerce between, . . . a place in the United States and any place outside thereof; whether such commerce moves wholly by aircraft or partly by aircraft and partly by other forms of transportation. (49 U.S.C. §1301(24)(c))

Section 403 of the Act provides:

> Every air carrier and foreign air carrier shall file with the Board, and print and keep open to public inspection, tariffs showing all rates, fares, and charges by air transportation between points served by it, and between points served by it and points served by any other air carrier or foreign air carrier when through service and through rates shall have been established. . . . (49 U.S.C. §1373(a))

In support of its argument that the VUSA fares are international fares, the Foreign Air Carriers rely upon a strict interpretation of the "flow of commerce" theory which provides that the characterization of transportation as foreign or domestic is determined by the intent of the shipper or passenger at the outset of the journey and is not affected by the occurrence of stopovers or other breaks in the transportation. (FAC Brief at 25-27) In support of its position, the Foreign Air Carriers rely on various court and Board precedents to argue that the Board has always

considered fares applicable between two foreign points which can be used in combination with fares to or from U.S. points to be within the Board's jurisdiction because they are fares in foreign air transportation of the United States within the meaning of the Act. (FAC Brief at 27-35) Thus, since the VUSA fares can be used only in combination with air transportation to or from the United States, they argue that the VUSA fares are fares "in foreign air transportation" and must be filed as international fares under section 403 and the tariff filing requirements of the bilateral agreements.

It is clear that the Board has not adopted the "flow of commerce" theory as advocated by the Foreign Air Carriers. Subjective passenger intent or flow of commerce is only one factor to be considered in the classification of traffic as foreign or domestic. In a recent proceeding, ER-1246, Tariff Flexibility, the Board rejected similar arguments made by IATA that Board precedent required that the ultimate origin and destination to define transportation as foreign or domestic. In that proceeding, the Board stated:

> In fact, we have rejected that test when necessary to preserve a fundamental policy of the Act . . . While some fares, those including stopovers for example, present special problems and uncertainties about the status of service between domestic points, these uncertainties need not preclude Board action. Rather, we believe that such questions can best be resolved on a case by case basis. (ER-1246 at 12)

On reconsideration of ER-1246, the Board reaffirmed its prior finding and stated:

> We reject a strict use of a flow of commerce test

> to define foreign air transportation in this context . . . IATA's assertion that our precedent uniformlly adopts such a rule is mistaken. Moreover, an examination of those precedents reveals that, had we adopted a flow of commerce test, it would have led to absurd results. Order 81-11-58 at 2.

In addition, the Board stated that, "Where innovative fares — like the Visit USA fares — raise new issues, resolution of these issues must of necessity depend upon the factual circumstances of each case." (Id. at 7). Even in the order on reconsideration of this proceeding, the Board stated flow of commerce is only one of the factors to be considered in deciding a particular case. (Order 82-1-83 at 3).

These recent determinations on the application of the "flow of commerce" test are not inconsistent with Board decisions made prior to the passage of the Airline Deregulation Act. For example, in *Qantas Empire Airlines Limited Foreign Transfer Traffic Case,* 29 CAB 33 (1959), the Board refused to apply the test where doing so would allow Qantas to carry passengers and cargo on the domestic segment of an international journey without providing transportation to the ultimate foreign destination. See also *Colonial Airlines, Inc., et al., Atlantic Seaboard Operation,* 4 C.A.B. 633 at 634 (1944); *Sitmar Cruises, Inc.,* Order 75-8-88 (1975). Even the Board case, *Canadian Colonial Airways, Inc., Montreal-Nassau Service,* 2 C.A.B. 752 (1941), relied upon by the Foreign Air Carriers is not an unqualified endorsement of the flow of commerce test. In classifying the journey involved in that case as foreign air transportation, the Board stated that the essential nature of the movement is determined by the ultimate destination. (*Id.* at 754). However, the Board went on to

limit its finding to the situation where "the stopover or interruption is merely an incidental part of the whole trip. . ." (Id.) The Board specifically found that the interruption involved in that case was for "safety reasons only" and that the stopover was "merely incidental to the through trip." (*Id.*)[17]

In further support of its argument, the Foreign Air Carriers assert that the Board has always considered fares applicable between two foreign points which can be combined with fares to or from U.S. points to be fares in "foreign air transportation" and within the Board jurisdiction. (FAC Brief at 27-31). In this regard, they cite various Board orders and decisions dealing with the question of whether the Board should grant anti-trust immunity for fare agreements filed with the Board by the International Air Transport Association under sections 412 and 414 of the Act.

Those cases are of little help in the determination of whether VUSA fares are foreign or domestic transportation. The Board's exercise of its regulatory jurisdiction in those cases was based on the effect of the IATA agreements on U.S. commerce. The Board exercised its antitrust authority under sections 412 and 414 to ensure that IATA's concerted action did not unduly impair the choices available to passengers or shippers in the United States.

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[17] In the *Settle* case relied upon by the Foreign Air Carriers, the Supreme Court stated that there are many instances where a local shipment follows quickly an interstate shipment and is not part of the interstate movement even though further shipment was contemplated at the origin point. *See Baltimore & O.S.W.R.R. Co. v. Settle* 260 U.S. 166 at 173 (1922). *See* also *Chicago, Milwaukee & St. Paul Ry. Co. v. Iowa* 233 U.S. 334 (1913).

The Board has never required the IATA carriers to file with the agency fares for transportation that is solely between two foreign countries. Such fares are not fares for "air transportation" under section 403 of the Act. The Board has ruled that, "absent agreements or other antitrust implications, however, we do not have jurisdiction over every foreign air fare a U.S. citizen may use or seek to use." Order 79-2-130 at 5. Combinable fares may affect foreign air transportation for section 412 and 414 purposes, but the transportation under them does not automatically become foreign air transportation under section 403 and the tariff filing requirements of the bilateral agreements.

The *IATA Europe-Israel Passsenger Fares Proceeding,* Order 78-7-113, is a case in point. In that case, the Board disapproved an IATA agreement to the extent that it prevented travel agents and air carriers from advertising or selling certain intra-European discount fares, from combining them with fares to or from the United States, and from selling them to U.S. citizens. The Board's action was based on its finding that these conditions were grossly discriminatory to Americans and adverse to the public interest because they caused Americans to pay higher through fares than were available to other travellers who purchased the lower intra-European fares separately by double ticketing. The offending portions of the IATA agreement were not granted anti-trust immunity. On reconsideration, the Board made it clear that it was not suggesting that carriers offering the fares had to file the fares with the Board unless they were part of a through trip to or from the United States. The Board emphasized that the fares-at-issue were not in air transportation, that they were subject to the jurisdiction of the countries to which the fares applied, and that the carriers could be subject to en-

forcement action by foreign governments which had not approved unrestricted fare sales. (Order 79-2-130 at 3, 5). In short the Board's action was based on the impact on U.S. foreign commerce and not the combinability of the fares.[18]

The Board has expressed the standard that is to be applied to this proceeding. In ER-1246 at 11, the Board stated:

> The term "foreign air transportation" as currently understood for the purposes of filing requirements under the Act and bilateral obligations is much more limited. It clearly covers tariffs for through fares for on-line service, joint fares for interline service and arbitraries used to construct interline fares to interior U.S. points. Such fares would not be affected by our rule and their filing will continue to be mandatory. Between such tariffs and purely domestic fares there may be fares that raise uncertainties; these are best analyzed on a case-by-case basis and in a specific factual context.

In Order 81-11-58, the Board reaffirmed this standard and applied it to this proceeding:

> Where innovative fares – like the Visit USA fares – raise new issues resolution of those issues must of necessity depend upon the factual circumstances of each case . . . [W]e . . . will exmaine new fares on a case-by-case basis. (Order 81-11-58 at 7).

[18]The foreign carriers have also relied upon a number of decisions by the Interstate Commerce Commission that a flow of commerce test should govern this issue. Those cases are not entitled to more weight than the Board's cases and are rejected.

See also Order 81-11-182 at 8. Applying this standard, I conclude that the VUSA fares at issue are international fares.

The VUSA fares at issue in this proceeding are novel and the resolution of their status as international or domestic has not been considered by the Board in any previous proceeding. On examination, they contain characteristics of both foreign and domestic fares. As discussed above, VUSA fares have been offered by various carriers for about 15 years. During this time, the carriers have always considered the VUSA fares to be domestic. When domestic fares were required to be filed with the Board, VUSA fares were filed in the carrier's domestic tariffs. VUSA tariffs were not filed with any foreign government nor does it appear that any foreign government ever questioned their status.[19] It was only about 1980 that the carriers under investigation began to place restrictions on their VUSA fares which provoked the foreign carriers' complaint.

The U.S. carriers and the Bureau argue that since VUSA fares cover only travel within the United States, the fares are not international but interstate transportation as provided for in section 101(24)(a). However, the argument disregards the fact that VUSA fares can be purchased only by residents of foreign countries. They cannot be purchased by individuals residing in the United States. The VUSA fares under investigation require the traveller to use the transoceanic service of the carrier offering the VUSA fare. Further, there can be little doubt that one of the primary

[19]There is evidence that the Delta VUSA fare is filed with the German Government (1 TR 151). The VUSA fares of American, Eastern, and United are not filed with the German government since Germany has no jurisdiction over carriers not operating in Germany. (*id.*)

reasons for instituting the restricted VUSA fare was to attract passengers to the carrier's international services.[20] At the hearing, TWA's witness testified that the VUSA fare is used to promote the carrier's transatlantic service:

Q: And is there also an advantage to requiring the Trans Atlantic portion to require online in the sense of the entire journey, the international and the domestic portion?

A: We think there is. We're not going to — we believe there is.

Q: What is that advantage?

A: We believe that the VUSA fare is a marketing tool, and that if we can offer total online service including the international and the U.S. travel, we think it gives the carrier offering that fare an advantage.

Q: In what market is that marketing tool — in what market do you see the advantage of that marketing tool?

A: Well, it would be an advantage in the market of passengers from foreign originations, foreign residents travelling to the U.S. and looking for an unlimited travel pass throughout the U.S. — that market.

Q: So the market in which this competitive marketing tool gives you an advantage is the international passenger market.

A: Trans Atlantic, yes (2 TR 168-69)

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[20] VUSA fares also have beneficial effects on the U.S. carriers' domestic system. But that is not the sole purpose for instituting the restricted VUSA fares.

See also 2 TR 191, 205, and 226; TW-IR-4. Even Northwest, on brief at 16, acknowledges that VUSA fares help attract passengers to the U.S. carriers' international services. Further, in an inter-office memorandum announcing its new VUSA fare, Capitol explained that, "It is felt that this new marketing tool will significantly stimulate travel to the U.S. and further on Capitol." (CL-IR-2 at 16).

The foreign carriers argue that VUSA fares are in reality international arbitraries used to construct through fares to interior United States points. (FAC Brief at 42-51) An arbitrary is defined as follows:

> Arbitrary means an amount published for use only in combination with other fares for the construction of through fares. It is also referred to as "Proportional Fare," "Basing Fare," and "Add-On-Fare"[21]

Arbitraries are published by air carriers for use in constructing a fare over a routing extending beyond the carrier's gateway point, for which no single factor rate is published. Acording to JAL and Lufthansa, the distinguishing feature of an arbitrary is that it is a fictitious or "paper" fare not available for purchase as published. This is certainly true of the VUSA fares at issue. Even though VUSA fares were published in a domestic tariff, they are not independently available for purchase; it can only be purchased in combination with an international trip on the transatlantic VUSA carrier. Further, the fact that VUSA fares entail certain characteristics, such as unlimited mileage, multiple stopovers, and circuity of routing, not

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[21]Tariff C.A.B. No. 376 issued by Airline Tariff Publishing Co. Agent, 6th revised page 2), effective July 26, 1982.

possessed by conventional "point-to-point" arbitraries, does not mean that the fares should be classified as domestic. The VUSA fares of TWA, Pan Am and Northwest offer essentially unlimited mileage beyond gateway transportation. Such fares are available only in combination with other fares for the construction of fares covering a through international journey, and are undistinguishable from arbitraries covering beyond gateway transportation.

The opposing parties all argue that VUSA fares are not arbitraries. Basically they argue that VUSA fares are not similar to traditional point-to-point arbitraries and that there is no identifiable turnaround point. The other parties assert that the way VUSA fares are used by the passengers demonstrates that they are not arbitraries. In this regard the Bureau and the U.S. carriers have prepared and cited detailed data concerning the routings and stopovers taken by VUSA passengers.[22] In the Bureau's view, this data is crucial in the determination of whether VUSA fares are international or domestic.

It is true that point-to-point arbitraries are clearly distinguishable from VUSA fares. And it is also true that VUSA fares do not have an identifiable turnaround point. However, I do not find this latter point to be fatal to classifying VUSA fares as international, and the U.S. carriers have not explained why it should be. Moreover, the fact that VUSA fares are characterized by stopovers and circuity of routing does not mean that VUSA fares are domestic fares. Indeed, it was conceded at the hearing that the Board has not used stopovers for circuity as criteria for determining whether a fare is in foreign air transportation. (3 TR at 51-53).

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[22]Much of this data was summarized *supra*. *See* also BIA Brief at 14-17.

In short, VUSA fares, which are unique and novel, may not be exactly like traditional international arbitraries, but they are very close. The restricted VUSA fares under investigation can only be purchased in combination with an international trip on the VUSA carrier. The VUSA program is restricted to the foreign nationals and cannot be purchased by the general public for transportation within the United States. Moreover, the overwhelming majority of VUSA tickets and itineraries are purchased and prepared at foreign originating points. Finally, VUSA fares are international fares because the intent of the passenger in purchasing the VUSA fare was to engage in an international roundtrip journey,[23] and that was the intent of the carriers offering the VUSA fare.

The U.S. carriers also argue that the stopovers that the VUSA passengers engage in amount to a clear and distinct break in the passenger's journey between his international and VUSA travel. I do not agree. The stopovers are planned stops in the VUSA traveller's itinerary, and the itinerary was planned prior to his departure from his foreign origination point. These stopovers do not alter the fact that the VUSA traveller is engaged in an integrated journey from a foreign point through the United States and back to his origin point.

The Bureau argues VUSA passengers use these fares to travel around the United States in the same way they would use any other U.S. discount fare or systemwide unlimited mileage fare available. (BIA Brief at 18). There is no substantial evidence of record to support this opinion. In fact, the Bureau's witness could not suggest any domes-

[23]The Board said that intent of the passenger could be one of the factors to be considered.

tic fares which offer unlimited stopovers or circuity of routing the way VUSA fares do. (3 TR 23-24).[24] Even if it could be shown that domestic discount fares would be used by passengers as a substitute for VUSA fares, that factor would not transform VUSA fares into domestic fares. For it is equally apparent that if point-to-point domestic arbitraries were unavailable, then passengers desiring to travel on such itineraries may use domestic point-to-point full fares and/or domestic discount fares to travel throughout the United States. However, this observation does not transform the point-to-point arbitraries, which are filed in international tariffs and are concededly international fares, into domestic fares.

The U.S. carriers also argue that VUSA fares are domestic because in their internal operations the revenues from VUSA are classified as domestic. In addition, they point out that VUSA fares are ticketed separately on domestic ticket stock. Such evidence does not detract from the fact that VUSA fares are part of a integrated international journey. To a large extent, such evidence is self-serving. Even the Bureau's witness testified that where the carriers place their VUSA revenues for accounting purposes should not be given any substantial weight. (3 TR 62-63) Further, it does not appear unusual for U.S. carriers to classify intra-U.S. sectors of international through fares as domestic for revenue accounting purposes. (2 TR 19-20). With respect to the use of domestic tickets, neither the Act nor any Board cases have relied on this fact as a basis for determining whether a fare is international or domestic. Again, the Bureau's witness acknowledged that

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[24]Eastern may offer a system excursion plan. (3 TR 23) No party has cited on brief any domestic fares that would offer the features of a VUSA fare.

a domestic fare combined with an international fare causes the transportation to be international. (3 TR 61). As noted, the restricted VUSA fares at issue can only be purchased by a passenger who holds a transoceanic ticket from the VUSA carrier.

Northwest, the Bureau, and the Department of Transportation argue that VUSA fares must be found to be domestic in order to achieve relevant policy goals of the Act. (Northwest Brief at 15-17; BIA Brief at 22-23; and DOT Brief at 7-8.) While such considerations are important, the evidence of record does provide any substantial basis to find that those policy goals will be hindered by a determination that the restricted VUSA fares are in foreign air transportation. The fares at issue are not all VUSA fares, but only the restricted VUSA fares of Northwest, Pan Am, TWA, and Capitol. Finding these fares to be international does not mean that discrimination by foreign governments will become the rule for VUSA fares as the U.S. parties appear to imply.

Finally, it should be noted that the VUSA fares at issue are distinguishable from the fares at issue in the *Tariff Flexibility Rulemaking,* ER-1246. In that proceeding, the fares at issue were generally and independently available for purchase by domestic passengers without reference to prior or subsequent travel on international flights. Restricted VUSA fares are not available to domestic passengers, but only to residents of foreign countries who travel to the United States on one of the four VUSA carriers. The fares at issue in both proceedings are completely different, and the Board's ruling in ER-1246 does not compel a finding that VUSA fares are domestic. As noted above, the impact of the restricted VUSA fares is in the marketing of the U.S. carriers' transoceanic service.

Accordingly, based on the evidence of record of how the restricted VUSA fares are actually applied, I conclude that the VUSA fares at issue should be classified as international fares under the Act and bilateral agreements.

UNJUST DISCRIMINATION

In the instituting order, Order 81-11-182, the Board asked whether the VUSA fares are unjustly discriminatory within the meaning of sections 404(b) and 1002 of the Act. In that order the Board noted that it had recently liberalized its policy on price discrimination and "status fares" (14 C.F.R. 399.96 adopted by Regulation PS-93, 45 Fed. Reg. 36058, effective June 27, 1980) and requested that evidence be developed so that findings concerning the VUSA fares could be made on each of the elements set forth in section 399.96. (*Id.* at 8) On reconsideration the Board reaffirmed its request with respect to section 399.96. (Order 82-1-83 at 5) Section 399.96 provides, in relevant part:

> (b) Except in unusual circumstances or as provided in paragraph (c) of this section, the Board will find a rate for domestic air transportation to constitute unreasonable discrimination only if:
>
> (1) There is a reasonable probability that the rate will result in significant long-run economic injury to passengers or shippers;
>
> (2) The rate is in fact discriminatory according to a reasonable cost allocation or other rational basis;
>
> (3) The rate does not provide transportation or other statutorily recognized benefits that justify the discrimination; and
>
> (4) Actual and potential competitive forces

cannot reliably be expected to eliminate the undesirable effects of the discrimination within a reasonable period.

(c) A rate that discriminates on the basis of the status of the traffic carried witll not be presumed to be unreasonably discriminatory, unless the use of the status categories in question is contrary to established national anti-discrimination policy.

The Foreign Air Carriers argue that the restricted VUSA fares violate section 404(b) (49 U.S.C. §1374(b)) in two distinct ways. First, the VUSA fare discriminates against the domestic carrier's non-VUSA passengers by giving a preference to those passengers who purchase a VUSA ticket by refunding a portion of their transoceanic fare while denying this discount to those passengers who do not purchase a VUSA ticket. As support for this argument, the Foreign Air Carriers rely upon *Complaint of Hawaiian Airlines, Inc. Against Aloha Airlines, Inc.,* Order 76-10-88, 71 C.A.B. 868 (1976), *affirmed sub. nom. Aloha Airlines, Inc. v. C.A.B.,* 598 F.2d 250 (D.C. Cir. 1979). Second, they argue that restricting the sale of VUSA fares to those passengers who use the U.S. carrier's services on the transoceanic sector constitutes discrimination against foreign-flag carriers' passengers based on the status of traffic. With respect to the Board's policy statement set forth in section 399.96, the Foreign Air Carriers argue that it is restricted to domestic air services and does not apply to foreign air transportation and is not applicable to the issues raised in this proceeding. In essence, the Foreign Air Carriers have made little effort to demonstrate that discrimination exists under the policy statement, and instead have relied upon legal precedent predating the policy statement.

In response the Bureau and the U.S. Carriers argue that the Foreign Air Carriers have ignored the Board's policy

statement, its request for evidence concerning each of the elements set forth in the policy statement, and that they have failed to carry their burden of proof.

The Board's Policy Statement — 14 C.F.R. 399.96

In the instituting orders, the Board clearly stated that it wished the parties to this proceeding to develop evidence with respect to the elements set forth in section 399.96. The Foreign Air Carriers have failed to comply with the Board's direction. Even though the Board has placed the policy statement in issue, the Foreign Air Carriers state that it is not applicable to the issues raised in this proceeding. (*See* FAC Brief at 88-90, FAC Reply brief at 44-45). Further, the Foreign Air Carriers have disregarded other recent Board cases which have adopted the policy statement to the international arena.

In the general policy statement (PS-93), the Board concluded that in view of the passage of the Airline Deregulation Act that it should reduce its interference in management decisions on differential pricing. Accordingly, it adopted a proposal to limit findings of unreasonable discrimination to cases where: (a) the fare or rate is in fact discriminatory without providing other benefits recognized under law; (b) the fare or rate is likely to result in long-run economic injury to passengers or shippers; and (c) the undesirable effects are not likely to be eliminated in a reasonable period of time without regulatory interference. (PS-93 at 2) Further, the Board eliminated the then-existing presumption against the legality of "status fares."

In PS-93, the Board stated that it "did not intend to preclude a common international pricing application," but limited the policy statement to domestic and overseas transportation. However, the Board went on to state:

> Nevertheless, the passage of the International Air Transportation Competition Act of 1979, after our initial policy proposal here, has substantially altered the statutory and policy framework within which we consider international pricing and entry issues. In many pertinent respects, the framework is now similar -- if not identical -- to the domestic area. While there are ad hoc circumstantial differences, such as limited entry in some international markets and detailed pricing control by a number of foreign governments, we believe that many of the fundamental policy considerations that lead us to issue this statement are equally applicable to foreign air transportation. (*Id.* at 9)

Further, the Board has applied the general policy statement in several other international fare cases. In *Lufthansa German Airlines v. Pan American World Airways,* Order 82-1-81, the Board considered Lufthansa's charges of unlawful discrimination in light of the pricing policy set forth in PS-93 and concluded that they must be rejected. In fact, the Board concluded that it was appropriate to apply the policy statement to the U.S.-Germany market since it is a "relatively competitive market" as a result of the procompetitive U.S.-FRG bilateral agreement of 1978. (*Id.* at 5). More importantly, in the *Pacific Common Fares Investigation,* Order 82-7-20, the Board found the general policy statement to be fully relevant to the consideration of international fares. (*Id.* at 12-13). In that case, the Board noted that consideration of the policy elements is necessary when the question of cost justification, competitive behavior, and consumer needs are at issue in an evidentiary proceeding. (*Id.* at 13) Those very questions are present in the VUSA proceeding.

Thus, it is clear that the Foreign Air Carriers have had ample notice that the Board would apply the general policy statement on price discrimination to international fares and rates. However, the Foreign Air Carriers argued that application of the policy statement to foreign air transportation can only be taken by formal rulemaking pursuant to the Administrative Procedure Act, 5 U.S.C. 500 *et seq.* (FAC Brief at 88). However, they have not cited to any particular statutory provision or precedent which would require the Board to engage in formal rulemaking. In fact, the APA exempts interpretative rules and general statements of policy from the rulemaking requirements. (5 U.S.C. §553)

In any event, the Board has established a new policy in PS-93 to deal with unjust discrimination and has directed that the new policy be applied in this proceeding. The purpose of the policy is to place greater reliance on competitive forces and reduce governmental interference with marketing decisions. In PS-93, the Board established four elements in order to support a finding of unjust discrimination. The foreign carriers have not demonstrated that the VUSA fares meet the standard.

First, they have not shown that there is a "reasonable probability" that the VUSA fares will result in "significant long-run economic injury to passengers." (14 C.F.R. 399. 36(b)(1)). The basis of the Foreign Air Carriers complaint is that their passengers cannot use the restricted VUSA fares of TWA, Pan American and Northwest because of the condition that passengers travel to the U.S. be on those carriers. However, it has been a long established principle of the Board "that there can be no unlawful discrimination, prejudice or disadvantage to the traffic of some other carrier." *Pan American Ferry Flight Case,* 18 CAB 214 at

221, n. 9 (1953); *Delta Off-Peak Coach Fares,* 39 CAB 377 at 391 (1963). The passengers of the Foreign Air Carriers could use the services of the other domestic carriers, such as Eastern or American, to purchase VUSA fares. Furthermore, the fact that Lufthansa carried more VUSA passengers than any other U.S. carrier demonsrates that its passengers are not suffering any long term injury. (NW-9 at 1).[25]

The Foreign Air Carriers have not shown that the VUSA fares are "in fact discriminatory according to a reasonable cost allocation or other rational basis." (14 C.F.R. 399.36(b)(2)) Little evidence has been submitted concerning individual carrier's and market costs. Such evidence is crucial to make a finding of unjust discrimination. *Pacific Common Fares Investigation,* Order 82-7-20 at 13.

The only evidence presented by the Foreign Air Carriers on this point was a computation of VUSA yields which show that TWA's, Pan Am's, and Northwest's yields are below its average system yield. (FAC-9)[26] Differing yields

[25]The record demonstrates that there are reasonable alternatives available to the VUSA fares of TWA, Pan American, and Northwest. For example, all of the 43 cities on Northwest's domestic system, are served by other U.S. carriers offering VUSA fares. (NW-8). Pan American's VUSA unlimited mileage VUSA fares are available not only to its foreign originating passengers but also to JAL's or Lufthansa passengers at the same fare level. (PA-R-1 and 2). The 12 cities accounting for 70 percent of all TWA VUSA boardings are also served by United, Eastern, Delta, and American whose VUSA fares are available to the transoceanic passengers of the foreign carriers. (BIA-R-1 at 5-6).

[26]The Foreign Air Carriers have also introduced comparisons of two TWA VUSA itineraries via point-to-point fares compared to TWA's VUSA fares (FAC-8) and a comparison of VUSA fares for TWA and Northwest versus the lowest unrestricted fares per mile. (FAC-10)

for differing fares are the norm today and have been encouraged by the Board when it adopted the general policy on price discrimination.[27] A showing of price or yield differentials alone will not be sufficient to establish a showing of discrimination.[28] The VUSA fares are competitive promotional offerings which encourage travel within the United States by foreign tourists as well as promote the transoceanic service of Pan Am, Northwest, TWA, and Capitol. These fares fill empty seats and contribute to revenues by inducing foreign originating passengers to travel on the carrier offering the VUSA fare or on one of the other participating carriers (2 Tr 130, 182, 228) In an economic environment in which competition is emphasized over regulation and in which carriers have been encouraged to experiment with competitive pricing practices (PS-93 at 4), it has not been demonstrated that there is no "reasonable cost allocation or other rational basis" for the VUSA fares.

Finally, the record of this proceeding does not provide a substantial basis to find that actual or potential competition cannot eliminate the effects of any discrimination within a reasonable time. As noted above, at least ten other U.S. carriers offer VUSA type fares which are available to the passengers of the foreign carriers in competition with the U.S. carriers involved in this proceeding. (BIA-R-5, 6, 7) The record demonstrates that the VUSA

[27]"Differential pricing to fill . . . unused capacity is a rational business response which, by spreading costs among more consumers, will actually reduce prices in a competitive environment." PS-93 at 8. "[W]e expect differential pricing to be a permanent feature of a competitive air transportation system as airlines attempt to satisfy simultaneously time-sensitive and price-sensitive passengers." *Id.* at 5.

[28]It is doubtful that such evidence would have been sufficient in the regulatory environment existing before the passage of the Airline Deregulation Act.

fares available to the foreign carriers have been used extensively by Lufthansa's passengers.[29] In 1981, in the U.S.-Germany market, Lufthansa carried approximately 8,800 passengers in comparison to Pan American's 8,039 passengers, TWA's 8,407 passengers, Capitol's 273 passengers, and Northwest's 182 passengers. (PA-R-9, ALJ-1, CL-IR-1, NW-IR-5). In addition, Lufthansa carried 1,340 passengers who participated in Pan Am's unlimited VUSA fare. (PA-R-2, 3, 9). Japan Air Lines failed to produce data on the number of passengers it carried, but it is clear that it did carry VUSA passengers. In fact, since February 20, 1981, passengers originating in Japan can use the transocean flights of JAL and participate in Pan Am's unlimited VUSA program at the same fare level as a passenger who uses Pan Am's transoceanic service. (PA-R-2, 3) Thus, it is clear that Lufthansa has been able or has had adequate opportunity to compete quite effectively for VUSA passengers in the U.S.-Germany market.[30]

Discrimination Against the U.S. Carrier's non-VUSA Passengers

As noted above, the Foreign Air Carriers argue that the restricted VUSA fares discriminate against passengers of Northwest, Pan Am, TWA, and Capitol who do not purchase a VUSA ticket by refunding a portion of the transocean fare to passengers who do purchase a VUSA ticket.

[29]In Order 82-1-81, the Board described the U.S.-Germany market as a "relatively competitive market" attributable in large part to the "procompetitive U.S.-FRG Bilateral" of 1978 (*Id.* at 5).

[30]The Foreign Air Carriers argue that the VUSA programs of other U.S. carriers are not practical alternatives because service and fares are noncomparable. As discussed in the section dealing with subissue (c), *infra,* I do not believe the record supports the foreign carriers' arguments.

(FAC Brief at 75-83). The foreign carriers rely upon *Complaint of Hawaiian Airlines, Inc. Against Aloha Airlines, Inc.*, 71 C.A.B. 868 (1976), affirmed in part *sub. nom. Aloha Airlines, Inc. v. C.A.B.*, 598 F.2d 250 (D.C. Cir. 1979) to support their arguments. None of the other parties addresses this issue directly except to state in a very general way that PS-93 overruled all precedents prior to its issuance and are no longer controlling law. This particular issue deserved better discussion. Decisions by the Court of Appeals cannot be dismissed so easily.

In the *Aloha Airlines* case, the Board found that a program instituted by Aloha in which its passengers could rent cars from Budget Rent-a-Car for seven dollars per day that were regularly priced at fourteen dollars per day to be illegal under the Act. Aloha argued that its payments to Budget under the program were for its *pro rata* share of advertising costs. However, the Board found that the evidence of record established that the payments had no relationship to advertising costs, but represented an agreed upon payment per rental contract and that the transaction constituted an unlawful rebating scheme, a departure from its published tariff. (71 C.A.B. at 870).[31]

On appeal, the Court of Appeals upheld the Board's decision in part. The Court of Appeals upheld the Board's finding that Aloha's payments subsidized Budget's discount rates and amounted to a fare rebate for passengers renting cars, and thus violated the Act. (598 F.2d at 250 *et seq.*). However, the Court noted that the original Aloha-Budget arrangement, described above, had been superseded by a new agreement between Aloha and Budget. Under the later agreement, Aloha made no payments to Bud-

[31]Under the program Aloha paid Budget over $1,350,000. At the same time, budget's advertising cost of the program was less than $360,000.

get on the basis of the numbers of cars rented to Aloha passengers nor did Aloha pay any part of the air fares collected to Budget. The Court found that the later arrangement was a legitimate joint business venture in which both parties sought an increase in business and each contributed to a joint promotion. Under the revised program, Budget continued to rent cars to Aloha passengers at reduced rates. In essence, Aloha paid for advertising of the programs and Budget reduced its rates to Aloha's passengers. The Court then set aside the Board's finding that the revised arrangement amounted to an illegal rebate or unjust discrimination. (*Id.* at 259-261).

I do not find that the *Aloha Airlines* case supports the foreign carriers' arguments. The foreign carriers do not distingusih between the two Aloha-Budget programs. How the VUSA program is identical to the illegal Aloha-Budget program, but dissimilar from the legitimate Aloha-Budget program is not explained. Further, the foreign carriers' argument that the U.S. carriers are rebating a portion of the transoceanic fare to its VUSA passengers is not supported by the record. There is simply no evidence that the U.S. carriers -- and the foreign carriers do not cite any — look to the transocean fare to make up for VUSA discounts.

As support for its assertion, the foreign carriers attempt to analogize TWA's VUSA program to the illegal Aloha-Budget program. TWA charges passengers of other carriers' $475 for a VUSA ticket that TWA's passengers pay $399. Thus, according to the foreign carriers, TWA is crediting or "rebating" $76 of the TWA passenger's fare in the form of an entitlement to purchase a TWA VUSA ticket. The foreign carriers' conclusion is without any basis, and without more, a finding of unjust discrimination cannot be found.

Discrimination Against Foreign Flag Carriers' VUSA Passengers

The Foreign Air Carriers also argue that restricting the sale of VUSA tickets to passengers who have used the U.S. carriers' services on the transocean sector constitutes unjust discrimination based on status of the traffic. (FAC Brief at 83-87) Relying upon the "rule of equality," the foreign carriers assert that the VUSA fares amount to fare discrimination based on the nature of the passenger's prior or subsequuent transportation which is illegal under section 404(b).

As noted above, in PS-93 the Board overturned the presumption that "status fares" are illegal. The Board has described "status fares" as "those fares based on personal characteristics of the traffic, such as youth fares or family fares." (PS-93 at 2). Such fares are generally "based on social factors such as age and status, not transportation-related factors, such as cost-savings." *Trailways of New England, Inc. v. Civil Aeronautics Board,* 412 F.2d 926 (1st Cir. 1969) *See* also *Transcontinental Bus System, Inc. v. Civil Aeronautics Board,* 383 F.2d 466 (5th Cir. 1967) *Cert. Denied* 390 U.S. 920 (1968). In PS-93, the Board determined that the rule of equality was no longer applicable to the airline industry, and determined that prior Board cases which enforced the rule were not to be strictly applied in the future. In its statement, the Board concluded.

> [T]he rule of equality is a rule designed to govern pricing practices of public utilities. Whatever relevance it might have had before the Airline Deregulation Act, we do not believe that, by itself, the rule requires the continuation of our historically stringent policies. (PS-93 at 8)

Recognizing that economic incentives could not be

relied upon to prevent certain types of invidious discrimination, such as the kind based on racial factors, religion or sex, the Board stated that such discrimination would still be presumptively illegal, and that its role would be "limited to maintaining these existing barriers to invidious discrimination." (*Id.* at 8-9)

VUSA fares are not fares based on "social factors" and do not qualify as "status fares". The alleged discrimination is based upon the fact that their restricted VUSA fares require the passenger to travel on the U.S. carriers' transoceanic service in order to purchase a VUSA ticket. The foreign carriers are not challenging the fact that the fares are available only to foreign residents. (FAC reply brief at 41).

As noted above, the Board has determined that changes in the airline industry require it to alter its longstanding presumption against "status fares" and to restrict its role to areas involving "invidious discrimination." VUSA fares clearly do not fall into the latter category. Furthermore, the cases cited by the foreign carriers do not support their assertion that the VUSA fare constitute a "status fare". Most of the cited cases involve classic "status fare" situations where the fares were based on "age" of the passenger. Accordingly, it is concluded that the foreign carriers have failed to demonstrate tht the VUSA fares are "status fares" that cause unjust discrimination.

Miscellaneous

In Order 81-11-182 at 8, the Board directed the U.S. carriers to distinguish the VUSA fares from the fares at issue in Orders 79-2-130, 78-7-113, and 80-10-25 or show why they should not be followed. (The U.S. carriers have barely attempted to comply with the Board's order in this re-

gard.) However, as noted by the Bureau, these decisions do not support a finding that the VUSA fares are unjustly discriminatory. In 78-7-113 and 79-2-130, the Board held that IATA carriers could not agree on a general rule to not sell special fares which were available between Europe and Israel. Carriers were not required to sell the fares to U.S. citizens. However, the Board found the agreement to refuse to disclose information about the special fares and to prohibit or discourage sales to U.S. citizens who could meet the same travel restrictions as non-U.S. travellers to be discriminatory.

Do the VUSA Fares Deny Foreign Air Carriers a Fair Opportunity to Compete?

In Order 81-11-182 at 9, the Board stated that this proceeding should explore whether the VUSA fares contravene the provisions of the bilateral agreements between the United States and the foreign countries of the complainants which ensure that the carriers of the signatory parties have a fair opportunity to compete in operating the agreed services. The Board stated further that evidence should be introduced of economic alternatives available to the complainants other than the VUSA fares of the U.S. carriers under investigation. In addition, the Board requested information which shows how the bilaterals are applied in the respective foreign countries and international practice with respect to similar fare issues. *See* also Order 82-1-83 at 4-5.

The Bilateral Agreements

Article 8 of the U.S.-Federal Republic of Germany bilateral Air Transport Services Agreement of 1955 (Exhibit BIA-IR-9A) provides:

> There shall be a fair and equal opportunity for the airlines of each contracting party to operate on any route specified in accordance with paragraph (2) of Article 2 of this Agreement.

In 1978, the U.S.-Germany bilateral was amended by a protocol which became effective on November 1 of that year. The 1978 protocol included a new Article 5 entitled "Fair Competition" which provided, in part:

> Each contracting party shall allow a fair opportunity for the designated airlines of both parties to compete in the international air transportation services covered by the Agreement and this Protocol.[32]

Article 10 of the U.S.-Japan bilateral Air Transport Services Agreement of 1952 (Exhibit BIA-IR-10A) provides:

> There shall be fair and equal opportunity for the airlines of both Contracting Parties to operate the agreed services on the specified routes between their respective territories.

Article 11(1) of the Bermuda II (BIA-IR-11) is substantially the same as the articles quoted above.

Positions of the Parties

Relying upon the precise terms of the agreements, the Foreign Air Carriers argue that their opportunity to compete on a "fair and equal" basis for traffic moving beyond gateway points can only be realized if the passengers are provided access to VUSA fares on the same basis as the passengers of TWA, Pan American, Capitol, and North-

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[32]The 1978 protocol did not delete Article 8 of the 1955 agreement. No party has argued what effect, if any, the 1978 protocol has had on Article 8 of the agreement between the U.S. and Germany.

west. The foreign carriers assert that restriction by U.S. carriers of the VUSA fares to on-line traffic when foreign carriers are prohibited by law from offering comparable service is a denial of a fair and equal opportunity to compete contrary to the bilateral agreements and therefore barred by sections 1102 and 411[33] of the Act regardless of whether VUSA programs of other U.S. carriers may be purchasd by the passengers of Lufthansa or JAL. (FAC Brief at 56-75, FAC reply brief at 48-69)

Morever, the foreign carries argue that the VUSA programs of the other U.S. carriers do not constitute a fair and equal opportunity to compete for several reasons. First, in order for the VUSA programs of other U.S. carriers to be adequate and competitive alternatives, those VUSA programs must be comparable with the restricted VUSA program of Northwest, Pan Am, and TWA either in terms of cities offered or in terms of reasonably efficient and economical routing. In the foreign carrier's view, the restricted VUSA programs of the carriers under investigation offer more of the city pairs which foreign residents want to visit than do the U.S carriers whose VUSA systems are available to Lufthansa and JAL passengers. Further, foreign residents who use the VUSA programs of American, Delta, Eastern, or United would have to endure time consuming and exhausting circuity of routing. Therefore, in the foreign carriers' opinion, such alternative systems do not constitute a "fair and equal opportunity" to compete.

Second, the foreign carriers argue that the unrestricted VUSA programs of other U.S. carriers must be available to JAL's and Lufthansa's passengers at the same price that TWA, Pan Am, and Northwest charge their on-line pas-

[33]As the Bureau correctly points out, section 411 is not at issue in this proceeding. (BIA reply brief at 10-11)

sengers for equivalent VUSA travel. They argue that a JAL passenger who uses the VUSA program of American or United would have to pay at least $250 more for a VUSA package which is comparable to the VUSA package available on-line with Northwest for $475. (FAC-R-5(rev.)) In addition, a Lufthansa passenger would have to pay $400 to $700 more than he would pay for the same intra-U.S. travel as a TWA VUSA passengers. (FAC-8)[34]

The U.S. carriers, the Bureau, and DOT argue that the foreign carriers have not been denied a fair opportunity to compete for the traffic at issue. On brief, the Bureau asserts that the agreements ". . . may not require the grant of opportunities that are exactly equal in every way . . ." (Bureau Brief at 25) Moreover, they argue that the record shows that there are economically and commercially viable alternatives offered by other U.S. carriers that the passengers of the foreign carriers can and have used. Further, the parties argue that the foreign carriers have not been denied any rights conferred by the bilaterals because JAL and Lufthansa have not suffered any traffic loss as a result of the VUSA programs. Finally, the other parties argue that any disadvantage suffered by the foreign carriers is their own fault since they have not attempted to work out a prorate agreement with the U.S. carriers so that JAL's and Lufthansa's passengers could use the restricted VUSA programs at the same fare level as the passengers of the U.S. carriers.[35]

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[34]As noted, Pan Am's unlimited VUSA is available to Lufthansa and JAL at the same fare level.

[35]The Bureau and the U.S. carriers also argue that that amount of traffic represented by VUSA passengers in the U.S.-Japan and U.S.-Germany markets is *de minimis*. While the data cited by the Bureau demonstrates that Lufthansa and JAL are in stong competitive positions, I have not relied on this argument for my recommendation. *See* discussion *supra*.

Discussion

No party has attempted to discuss in detail how the articles of the bilaterals should be interpreted. Except for references to Board cases cited by the foreign carriers, no party has attempted to detail how the bilateral provisions are applied in foreign countries and international practice as the Board directed. However, it is not enough to cite the language of the agreement alone. In essence, that is all the foreign carriers have offered as support for their position. They have not provided any basis for this extreme interpretation of the bilateral agreements. Without more, I do not believe that their position can be upheld.

Neither the government of Japan nor Germany has protested that the restricted VUSA fares are in violation of the bilateral agreements. The governments are the contracting parties to the agreements which provide for consultation and settlement of disputes. Yet there is no evidence of record that Germany or Japan has sought such procedures with respect to the VUSA fares at issue. If the bilateral agreements required the interpetation that the foreign carriers are attempting to apply, then their actions would be supported by their respective governments. Further, it is noteworthy that British Airways does not agree with JAL's and Lufthansa's position. On brief, British Airways stated that the VUSA fares are not unlawful *per se* under the Act or the bilateral agreements. In that carrier's view, in the absence of significant market power by the U.S. carriers,

> [I]t may be assumed that there are adequate competitive alternatives to the restricted VUSA fare. A foreign carrier such as British Airways can presumably make alternative arrangements with another U.S. carrier, even at the cost of some subsidy to that U.S. carrier's VUSA fare, to meet the competition of a restricted VUSA fare. (British Airways brief at 4)

There is no evidence that the four U.S. carriers possess such significant market power. In fact, the evidence of record indicates that in transoceanic service, the foreign carriers control a larger share of the traffic than any single U.S. carrier. (BIA-IR-3; 3 TR 7) Also there is no evidence of any conspiracy among Pan Am, TWA, Northwest or Capitol.

Lufthansa and JAL have participated in Pan Am's unlimited mileage VUSA fares since February 1981 (PA-IR-1), and passsengers originating in either Japan or Germany, who use JAL or Lufthansa for the international journey, can purchase Pan Am's unlimited mileage VUSA fare at the same fare level as a passenger who travels on Pan Am for the transocean journey. (PA-R-2 and R-3) Further, JAL and Lufthansa do not pay any prorate dilution. (2 Tr 122; PA-IR-3; PA-R-3 and 4) In addition, JAL and Lufthansa participate in the system-wide unlimited mileage VUSA fares of American, Delta, Eastern and United. The evidence in the record demonstrates that these U.S. carriers do provide a reasonably available, practical alternative to the VUSA fares under investigation. While every carrier has some points that another carrier may not serve, American, Delta, Eastern and United do serve the great majority of cities that VUSA passengers travelling on Northwest, Pan Am and TWA visit. Indeed, these four carriers each serve more cities in the United States than either TWA, Pan Am or Northwest. (TW-D-2 through 7; NW-8; FAC-SR-1, p. 4) In addition Republic and Continental also have system-wide VUSA fares that also serve the great majority of cities that VUSA passengers desire to visit. (PA-12; NW-10)

That these VUSA fares are reasonably available alternatives to the VUSA fares under investigation is demonstrated by the amount of competition offered by these

carriers at the leading cities that the VUSA passengers of Northwest, Pan Am and TWA actually visit. TWA has computed that 12 of its 50 domestic cities account for 70 percent of its VUSA boardings. (TW-IR-2) Eastern and American serve all 12 of these cities. (TW-D-8) Delta and United serve all but St. Louis, (TW-D-8) and Republic serves all but Pittsburgh. (NW-R-1) St. Louis is used more as a "hub" connecting point by the VUSA passenger to stay on TWA's system than a point to be visited on its own. (1 Tr 193; 2 Tr 243; BIA-R-1, p. 3) Therefore, a typical VUSA passenger could visit all of the major TWA VUSA destinations on the systems of American, Delta, Eastern and United, and all but Pittsburgh on Republic. Eight cities represented 73 percent of the stopovers reflected in the itineraries used by Northwest's actual passengers. (NW-1; BIA-R-3 and 4) United serves all eight of these cities. American, Continental, Delta, Eastern, and Republic serve all of the cities except Honolulu. (BIA-R-5) American, Delta, Eastern, Republic and United serve all nine of the Pan Am destinations that account for 69 percent of Pan Am's VUSA passengers. (BIA-R-6; NW-R-1)

A comparison of the number of Lufthansa VUSA passengers who purchased the VUSA fares of American, Eastern and United with the number of VUSA passengers carried by Capitol, Northwest, Pan Am and TWA demonstrate that the other VUSA fares are a viable alternative to the VUSA fares under investigation.[36] Lufthansa showed that from July 1,1980 through June 30, 1981, it carried 8,800 passengers on American (4,200), Eastern (1,300) and

[36]There is no date in the record about the usage of VUSA fares in the U.S.-U.K. market. The only data for the U.S.-Japan market is for the U.S. carriers. As noted, JAL failed to provide comparable data, and it must accept the conclusions that can be drawn from the evidence supplied by the other carriers.

United (3,300). (FAC-IR-3) In addition, 1,304 Lufthansa passengers who purchased VUSA fares on Pan Am (PA-R-9) for a total of 10,104 passengers.

During this same time Northwest carried 182 passengers between Germany and the United States (NW-IR-5, p. 1), Capitol carried 273 passengers (CL-IR-1), and Pan Am carried 4,795 unlimited mileage VUSA passengers. (PA-R-9) TWA carried 8,407 VUSA passengers in the Frankfurt-New York market. Through the use of the VUSA fares of America, Eastern and United, Lufthansa has been able to carry more VUSA passengers in the U.S.-Germany market than any U.S. carrier. In fact, the number of Lufthansa passengers who used American alone was almost equal to the total number of passengers who used Pan Am's unlimited mileage VUSA fare. The conclusion remains the same if an analysis is made of the single-plane or on-line service provided by other U.S. carriers in the principal segments set forth in PA-11 that represent 69 percent of Pan Am's VUSA passengers. Even in these segments the system-wide VUSA fares of American, Delta, Eastern and United provided an alternative to the VUSA fare of Pan Am. (BIA-R-7) Eastern, for example, provides single-plane or on-line service in all but two of the segments served by Pan Am. Delta serves all except for three.

This conclusion is supported further by reviewing the service provided by other U.S. carriers in the cities that Lufthansa and JAL used in their sample itineraries. (FAC-T-1 (LH), FAC-T-2 (JL), FAC-8 and FAC-SR-15)[37] All of

[37]These itineraries are not actual itineraries traveled on the three carriers, but are hypothetical constructions based on Lufthansa's VUSA passengers traveling on American, Eastern, and United. (1 TR 122-126) In addition, the TWA hypothetical itinerary appears less circuitous than actual TWA sample itineraries. (BIA-R-2) Finally, there are three sectors (Atlanta-New Orleans, Chicago-Miami and Atlanta-

the points represented in these itineraries are served by at least one of the four U.S. carriers that interline with JAL and Lufthansa, and most are served by more than one carrier. For example, American and Eastern serve all of the cities listed in the itineraries in FAC-T-1 (LH) and FAC-8. Delta and United serve all of the points, except the connecting point of St. Louis, and except Albuquerque, which is not one of the leading cities visited by TWA's VUSA passengers. (TW-D-8) All four U.S. carriers serve the cities listed on the hypothetical Pan Am itinerary in FAC-T-(LH). Both Eastern and Republic serve all the cities on the hypothetical Northwest itinerary while Delta, Eastern and American serve all the points except two (TW-D-3-6; NW-R-1, 2; BIA-R-1 at 6). American, Delta, Eastern and Continental serve all the points on the Northwest itinerary in FAC-T-2 (JL) except for Honolulu. Further, the VUSA passenger can also fly that itinerary on United and Western. (NW-R-2)

The foreign carriers argue that the VUSA fares of the other U.S. carriers are not viable alternatives because a JAL or Lufthansa passenger could not travel over the same city-pair routings and itineraries that a passenger travelling on Northwest, Pan Am or TWA could use. The foreign carriers appear to conclude that only nonstop or direct service over the exact segment served by Northwest, Pan Am or TWA counts as an alternative since other routings involving connecting service are unduly more circuitous. As noted above, VUSA passengers actually use indirect circuitous routings that often involve multiple connec-

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Miami) listed in the Northwest itinerary over which Northwest is no longer providing nonstop service. The first two are available only with a layover via Minneapolis and the latter is available only with an overnight at Tampa or Orlando. In addition, the Miami-New York segment is served only once a week. (2 TR 7, 8)

tions or backhauls, and travel via hubs such as Minneapolis and St. Louis, to visit the cities that they want to see. Indeed, one of the foreign carriers' witnesses, recognized that VUSA passengers do endure circuity in order to save money (1 TR 210), and "will travel throughout the U.S. by subjecting themselves to Northwest's circuitous routings, necessitating repeated transfers at MSP." (FAC-SR-1) The foreign carriers' arguments are contrary to the evidence.

The foreign carriers also argue that the VUSA fares of the other U.S. carriers are not competitive alternatives because they would cost their passengers approximately $76 more than a passenger travelling on the VUSA fares under investigation (FAC-SR-1, p. 6; FAC-SR-13), and in the case of Honolulu, $250 more than a passenger using Northwest's VUSA pass. (FAC-R-5; FAC-SR-1, p. 6) They argue that even $76 is a significant amount to potential passengers, as evidenced by the foothold gained by Capitol in the New York-Zurich market with a fare differential of $85 under Swissair's fare. (FAC-R-6)

The record demonstrates that these price differentials do not place the foreign carriers at a competitive disadvantage. Capitol's $85 price advantage gained it a *de minimis* share of the New York-Zurich market in 1981. (BIA-IR-1, p. 2) What conclusively proves that the VUSA fares of American, Eastern, United and the other U.S. carriers are in fact viable competitive alternatives to the VUSA fares under investigation is that Lufthansa carried more VUSA passengers in the U.S.-Germany market that used these higher priced VUSA fares than any single one of the U.S. carriers under investigation.

As noted by the Bureau, the other U.S. carriers, and British Air, there is an alternative available to JAL and Lufthansa. They can do what many other foreign carriers

do to reduce the level of fares paid by their VUSA passengers; they can negotiate agreements with U.S. carriers under which they would agree to pay the $76 fare differntial as a prorate payment. (NW-10) Prorate agreements are a standard industry practice, and the record does not indicate that JAL and Lufthansa have made any attempt to work out any sort of agreement with the carriers offering restricted VUSA fares. (NW-IR-1, p. 3) Instead they are asking the Board to intervene in the marketplace to give them an advantage that other foreign carriers do not have. The United States' obligations under the fair opportunity to compete provisions of the bilateral agreements do not compel such action. Therefore, the contentions that JAL and Lufthansa are deprived of a fair opportunity to compete should be rejected.

Discrimination Abroad Against U.S. Carriers

Northwest and TWA has also alleged that they are subjected to unfavorable competitive situations in G ermany and Japan. In NW-7 Competitive Practices Exhibit,[38] Northwest cites a number of situations which it describes as "competitive obstacles" in Germany and Japan. (Northwest brief at 25, fn. 22). For example, Northwest cites the fact that JAL and Lufthansa are owned in part by their respective governments. However, on cross-examination, Northwest's witness admitted that the situations cited were not unfair or all that unusual. (*See* 2 TR 59-92) In addition, TWA also alleges that it was subject to a restrictive fare policy of the German government. On analysis, the matter is not a restrictive practice of the German government, but appears to be a management decision of TWA. (*See* 2 TR 214). TWA does not even raise the matter in its brief.

[38]NW-7 begins with page number 26 and ends with page 88. (2 TR 58)

Export-Inland Contract Rate

In April 1981 Northwest entered into two contracts, called the Export-Inland Contracts, for the carriage of freight over the Chicago to Seattle sector of a movement destined to a point in the Orient. (NW-IR-6) These rates were in effect for about six months. Under the agreements, the shippers paid a rate of six cents per pound for the Chicago-Seattle sector as long as they shipped a minimum of 300 metric tons of cargo within a 180 day period. (*Id.*, NW-IR-7).[39] There was no maximum limit on the amount of cargo that could be shipped under the contract rate, and both shippers met the minimum requirements. (NW-IR-7).

JAL argues that the contract rate is a rate in foreign air transportation which must be filed with the United States and foreign governments and is an illegal rebate in violation of section 404(b). Northwest responds that the contract rate involved solely domestic movements; there was a "break in the journey" between the domestic and international movements; and that it was not discriminatory.[40] The Bureau concurs in Northwest's position.

International v. Domestic

While there are strong arguments on both sides that the VUSA fares are international or domestic fares, there is little doubt that the Export-Inland Contract rates are rates in foreign air transportation. The evidence of record, which is made up mostly of Northwest's information re-

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[39]The 300 metric tons was reduced to 180 metric tons. (NW-IR-6 at 11).

[40]Northwest also argues that the complaint is moot. The complaint is not moot. *See* Order of the Administrative Law Judge of October 28, 1981. Evidently, the Board did not believe the issue was moot when it consolidated this proceeding and the VUSA proceeding. (Orders 81-11-182 and 82-1-83).

sponses and exhibits, is clear that the intent and effect of the contract rates was to enhance Northwest's competitive position in an international market.

In 1981, Northwest was informed that Korean Airlines and China Airlines were paying up to 18 percent additional commissions for transpacific international freight originating in the Chicago area. (NW-IR-7, *see* also NW-IR-9)[41] Northwest learned from its major shippers that these new commissions by the foreign carriers were diverting trraffic away from Northwest, and in order to regain the lost traffic Northwest proposed the Export-Inland contract rate to several large shippers. (*Id.*) Thus, the contract rate was instituted as a competitive response to a change in the commission structure of two foreign air carriers not domestic competitors.

The language of the contracts reinforce my determination that the rates are international rates. The contracts state that the "rates are applicable *only to international shipments* which terminate in . . . Hong Kong, Japan, South Korea, Phillippines, or Taiwan." (NW-IR-6 at 1, emphasis added). The contract also requires that the domestic air bill covering the movement from Chicago to Seattle include a signed endorsement that the shipment is a "true international shipment beyond the SEA gateway." (*Id.* at 1 and 3). In addition, an internal Northwest document, NW-IR-9, states that the rate is to be used for "transpacific rate construction purposes." This same document states that the contract rate should help Northwest remain competitive without altering its discount structure

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[41]NW-IR-9 has been accorded confidential treatment under Rule 39. In addition, a confidential oral hearing has also been held on the contract rates. (1 TR 84-101) Any portions of NW-IR-9 or the confidential transcript quoted herein deemed not to qualify for confidential treatment under Rule 39.

or "discounting off filed international rates" (*Id.*) Finally, at the hearing, Northwest's witness conceded that the rate was instituted to meet competition in the movement of international cargo from Chicago to the Orient. (1 TR 90) Thus, Northwest's arguments that the contract rate was its method of competing for domestic cargo is rebutted by its own exhibits.

Northwest argues that even under the flow of commerce test there was a "legitimate" 'break in the journey' at the Seattle gateway" which requires the contract rate movement to be classified as a domestic rate. According to Northwest, the break occurred when the traffic from Chicago was consolidated at Seattle with traffic from other points in the United States for the international movement. Northwest could not provide a solid estimate for the elapsed time between arrival in Seattle and departure for the Orient, but believed that at least 24 hours elapsed. (NW-IR-7 at 2-3). However, Northwest's witness, who sponsored NW-IR-7, acknowledged that he did not know if any shipments were ever consolidated or off-loaded for transshipment at Seattle (1 TR 73-76; 99). In fact, he did not actually know if there had been any delay at all in Seattle. (1 TR 65) In addition, the 24-hour estimate does not refer only to Export-Inland contract traffic, but applies to all traffic coming into Seattle. (1 TR 95-96)

Whatever delay occurred at the consolidation point, there is no substantial evidence of record that it was so significant as to constitute a break in the journey from Chicago to the Orient. Northwest's speculation about a break is not supported by the record. In fact, evidence in confidential NW-IR-9 and the confidential transcript indicate that whatever off-loading of cargo that occurred was minimal. (*See* NW-IR-9 at 3, 1 TR-85-86). Such pauses do not affect the nature of the movement as foreign air transportation.

See Canadian Colonial Airways, Montreal-Nassau Service, 2 CAB 752 (1941); *Foreign Off-Route Charter Service Investigation,* 27 C.A.B. 196 at 236 (1958) and *Bader Bros. Van Lines,* Order 74-6-110 (1974).

The Bureau appears to place substantial reliance on the fact that the contract rate was at the same level as an existing domestic rate (1 TR 64, 70, 71), and that the contracts were subject to the domestic cargo tariff rules and regulations. These are not substantial reasons to classify the contract rate as domestic and fly in the face of Northwest's and the shippers clear intent in entering into the contract rate. In addition, Northwest's reliance on the *Sitmar Carriers, Inc.,* Order 75-8-88, is misplaced. (Northwest brief at 26). There is no evidence that any contract traffic moved to the Orient by sea. In *Sitmar,* the Board indicated that if the traffic had moved by air instead of by sea between the United States and the foreign point, it would have reached a contrary conclusion. Even though the contract provides for transpacific movements by sea or carriers other than Northwest, the record is clear that all transpacific movements were performed by Northwest. (1 TR 98).

The Export-Inland Contract rate is really an arbitrary or an "add-on" to an international rate since it is an amount to be used only in combination with other rates for the construction of a through rate.[42] Northwest has filed such rates with the Japanese and United States aviation authorities. (1 TR 60) There is little to distinguish the contract rate from other arbitraries. It is a fare for use only in combination with transpacific rates from Seattle to the

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[42]It appears that Northwest's Vice President of Sales described the contract rate as a "paper rate" on at least one occasion. (1 TR 88, NW-IR-9)

Orient for the construction of a through rate to the Orient. Unlike the VUSA fares, factors such as unlimited mileage, circuity, and unlimited stopovers do not affect consideration of its classification. The contract rate is a point-to-point "add-on" and is in foreign air transportation.

Finally, it should be noted that there is evidence in the record that other U.S. carriers offer rates which may be used only in combination with international rates, but which are not filed with the Board or any foreign governments. (NW-IR-8). However, the data in the record is limited,[43] and does not affect my recommendation with respect to the Export-Inland Contract rate. The fact that other airliners offer rates which may be similar to the contract rate under investigation does not affect the circumstances and details of the contract rate which demonstrate that it is in foreign air transportation.

Unjust Discrimination

JAL argues that the Export-Inland Contract rate serves to rebate to certain shippers using Northwest's transpacific service a portion of the governmentally-approved rate they have paid for such transportation in the form of lower transportation costs from Chicago to Seattle. By using the contract rate plus the Seattle-Orient rate to construct a through rate, Northwest charged less than the published tariff through rate, thereby rebating a portion of the published rate. In JAL's view, this constitutes unjust discrimination and cites the *Aloha* case for authority.

Northwest responds that the rate was not unjustly discriminatory because the contract rate was available for

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[43]The rates of the other carriers do not appear to be restricted in terms of the carrier on which the international shipment moves.

shipments moving by foreign carriers. Further, whatever discrimination that may have existed was eliminated by the competition from other carriers who offered similar rates for domestic cargo moving to gateways for international consolidation.

In the instituting order, the Board stated that it wanted evidence developed so that findings concerning the VUSA fare and Export-Inland Contract rates could be made on each of the elements set forth in section 399.36. As noted above, the Foreign Air Carriers do not believe that the Board's policy statement on price discrimination is applicable to this proceeding. With respect to the contract rates, they have not even discussed on brief the Board's policy. Only Northwest has referred to the elements of section 399.36.

There has been no demonstration that the rate will cause shippers any long-run economic injury. In fact the contract rate was a reduced rate offered to shippers after China and Korean Airlines had reduced its commissions. Moreover, the rate was terminated in September 1981 and is no longer in effect.

The foreign carriers have not shown that the rate is discriminatory based on a reasonable cost allocation. There is no evidence in this element at all. In fact, the record shows the contracted rate was at the same level as an existing domestic rate (1 TR 64, 70, 71) Further, the only evidence concerning any harm JAL may have suffered is a statement that, during the six months that the contract rate was in effect, JAL's traffic for the Chicago-Japan market declined by 11 percent compared to the same period in 1980. Revenues for the same period declined by 6.1 percent. (FAC-T-3 at 3-5) However, the record does not show if this decline was caused by the contract rate. Finally, the

foreign carriers have not demonstrated that the contract rate falls within the last two elements of the policy statement.

Fair Opportunity to Compete Under the Bilateral Agreement

JAL has not argued on brief that the contract rate denied it a fair opportunity to compete under the bilateral ageement between the United States and Japan. The record demonstrates that it was not. The contract rate applied to only two shippers. There is no evidence that those two shippers controlled the entire or even a substantial volume of the Chicago-Japan market for cargo. Further, while it is true that JAL had to reduce its rates to match the contract rate, JAL exercised its right to compete as guaranteed by the bilateral agreement. That is all it can reasonably expect.

Ultimate Findings and Conclusions

Based upon the discussion above and all the facts of record, it is found that:

(1) the Visit USA fares and the Export Inland Contract rates at issue in this proceeding should be classified as international fares and rates under the Act and the civil air transport agreements;

(2) the Visit USA fares and Export Inland Contract rate at issue in this proceeding are not unjustly discriminatory within sections 404(b) and 1002 of the Act; and

(3) the Visit USA fares and Export Inland Contract rate at issue in this proceeding are consistent with the civil air

transport agreements which guarantee a fair opportunity to compete.

/s/ John M. Vittone
John M. Vittone
Administrative Law Judge

June 1, 1983

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APPENDIX D

FEDERAL AVIATION ACT OF 1958, AS AMENDED [49 U.S.C. §§1301 *et seq.*]

Definitions

SEC. 101. As used in this Act, unless the context otherwise requires—

* * *

(23) "Interstate air commerce", "overseas air commerce", and "foreign air commerce", respectively, mean the carriage by aircraft of persons or property for compensation or hire, or the carriage of mail by aircraft, or the operation on navigation of aircraft in the conduct or furtherance of a business or vocation, in commerce between, respectively—

(a) a place in any State of the United States, or the District of Columbia, and a place in any other State of the United States, or the District of Columbia; or between places in the same State of the United States through the airspace over any place outside thereof; or between places in the same Territory or possession of the United States, or the District of Columbia;

(b) a place in any State of the United States, or the District of Columbia, and any place in a Territory or possession of the United States; or between a place in a Territory or possession of the United States, and a place in any other Territory or possession of the United States; and

(c) a place in the United States and any place outside thereof;

whether such commerce moves wholly by aircraft or partly by aircraft and partly by other forms of transportation.

(24) "Interstate air transportation", "overseas air transportation", and "foreign air transportation", respectively, mean the carriage by aircraft of persons or property as a common carrier for compensation or hire or the carriage of mail by aircraft, in commerce between, respectively—

(a) a place in any State of the United States, or the District of Columbia, and a place in any other State of the United States, or the District of Columbia; or between places in the same State of the United States through the airspace over any place outside thereof; or between places in the same Territory or possession of the United States, or the District of Columbia;

(b) a place in any State of the United States, or the District of Columbia, and any place in a Territory or possession of the United States; or between a place in a Territory or possession of the United States, and a place in any other Territory or possession of the United States; and

(c) a place in the United States and any place outside thereof;

whether such commerce moves wholly by aircraft or partly by aircraft and partly by other forms of transportation.

[49 U.S.C. § 1301.]

* * *

TARIFFS OF AIR CARRIERS

FILING OF TARIFFS REQUIRED

SEC. 403.[1] (a) Every air carrier and every foreign air carrier shall file with the Board, and print, and keep open

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[1]Section 403 authority terminated January 1, 1983, to extent provisions relate to interstate and overses air transportation of persons. [sic] Section 1601(a)(2)(A) of this Act. [sic]

to public inspection, tariffs showing all rates, fares, and charges for air transportation between points served by it, and between points served by it and points served by any other air carrier or foreign air carrier when through service and through rates shall have been established, and showing to the extent required by regulations of the Board, all classifications, rules, regulations, practices, and services in connection with such air transportation. Tariffs shall be filed, posted, and published in such form and manner, and shall contain such information, as the Board shall by regulation prescribe; and the Board is empowered to reject any tariff so filed which is not consistent with this section and such regulations. Any tarifff so rejected shall be void. The rates, fares, and charges shown in any tariff shall be stated in terms of lawful money of the United States, but such tariffs may also state rates, fares, and charges in terms of currencies other than lawful money of the United States, and may, in the case of foreign air transportation, contain such information as may be required under the laws of any country in or to which an air carrier or foreign air carrier is authorized to operate.

[49 U.S.C. §1373(a).]

* * *

Judicial Review of Orders

ORDERS OF BOARD AND ADMINISTRATOR SUBJECT TO REVIEW

SEC. 1006. (a) Any order, affirmative or negative, issued by the Board or Administrator under this Act, except any order in respect of any foreign air carrier subject to the approval of the President as provided in section 801 of this Act, shall be subject to review by the courts of ap-

peals of the United States or the United States Court of Appeals for the Distict of Columbia upon petition, filed within sixty days after the entry of such order, by any person disclosing a substantial interest in such order. After the expiration of said sixty days a petition may be filed only by leave of court upon a showing of reasonable grounds for failure to file the petition theretofore.

VENUE

(b) A petition under this section shall be filed in the court for the circuit wherein the petitioner resides or has his principal place of business or in the United States Court of Appeals for the District of Columbia.

[NOTICE TO BOARD OR ADMINISTRATOR; FILING OF TRANSCRIPT][1]

(c) A copy of the petition shall, upon filing, be forthwith transmitted to the Board or Administrator by the clerk of the court, and the Board or Administrator shall thereupon file in the court the record, if any, upon which the order complained of was entered, as provided in section 2112 of title 28, United States Code.

[POWER OF COURT][2]

(d) Upon transmittal of the petition to the Board or Administrator, the court shall have exclusive jurisdiction to affirm, modify, or set aside the order complained of, in whole or in part, and if need be, to order further proceedings by the Board or Administrator. Upon good cause

[1]Subsection heading not reinserted by amendment of subsection Public Law 86-546, §1.

[2]Subsection heading not reinserted by amendment of subection Public Law 87-225, §2.

shown and after reasonable notice to the Board or Administrator, interlocutory relief may be granted by stay of the order or by such mandatory or other relief as may be appropriate.

FINDINGS OF FACT CONCLUSIVE

(e) The findings of facts by the Board or Administrator, if supported by substantial evidence, shall be conclusive. No objection to an order of the Board or Administrator shall be considered by the court unless such objection shall have been urged before the Board or Administrator or, if it was not so urged, unless there were reasonable grounds for failure to do so.

CERTIFICATION OR CERTIORARI

(f) The judgment and decree of the court affirming, modifying, or setting aside any such order of the Board or Administrator shall be subject only to review by the Supreme Court of the United States upon certification or certiorari as provided in section 1254 of title 28, United States Code.

[49 U.S.C. §1486.]

* * *

INTERNATIONAL AGREEMENTS

ACTIONS OF THE BOARD AND OF THE SECRETARY OF TRANSPORTATION

SEC. 1102. (a) In exercising and performing their powers and duties under this Act, the Board and the Administrator shall do so consistenlty with any obligation assumed by the United States in any treaty, convention, or agreement that may be in force between the United States

and any foreign country or foreign countries, and shall take into consideration any applicable laws and requirements of foreign countries and the Board shall not, in exercising and performing its powers and duties with respect to certificates of convenience and necessity, restrict compliance by any air carrier with any obligation, duty, or liability imposed by any foreign country; *Provided,* That this section shall not apply to any obligation, duty, or liability arising out of a contract or other agreement, heretofore or hereafter entered into between an air carrier, or any officer or representative thereof, and any foreign country, if such contract or agreement is disapproved by the Board as being contrary to the public interest.

[49 U.S.C. §1502.]

APPENDIX E

AIR TRANSPORT SERVICES

Agreement, with Schedule between the
UNITED STATES OF AMERICA AND JAPAN

- Signed at Tokyo August 11, 1952
- Entered into force September 15, 1953; provisionally in force August 11, 1952

and

Supplementing and Amending Agreements

- Effected by Exchanges of Notes
- Signed at Tokyo August 11, 1952
  Entered into force August 11, 1952
- Signed at Tokyo September 15, 1953
  Entered into force September 15, 1953

[4 UST 1948; TIAS 2854; 212 UNTS 27.]

* * *

ARTICLE 13

(A) The determination of rates in accordance with the following paragraphs shall be made at reasonable levels, due regard being paid to all relevant factors, such as cost of operation, reasonable profit, and the rates charged by any other airlines, as well as the characteristics of each service.

(B) The rates to be charged by the airlines of either Contracting Party between points in the territory of the

United States and points in the territory of Japan referred to in the attached Schedule shall, consistent with the provisions of the present Agreement, be subject to the approval of the aeronautical authorities of the Contracting Parties, who shall act in accordance with their obligations under the present Agreement within the limits of their legal powers.

(C) Any rate proposed by the airline or airlines of either Contracting Party shall be filed with the aeronautical authorities of both Contracting Parties at least thirty (30) days before the proposed date of introduction; provided that this period of thirty (30) days may be reduced in particular cases if so agreed by the aeronautical authorities of both Contracting Parties.

* * *

APPENDIX F

AIR TRANSPORT SERVICES

Interim agreement between the United States of America and Switzerland respecting air transport services. Effected by exchange of notes signed at Bern August 3, 1945; effective August 3, 1945.

[60 Stat. 1935; TIAS 1576; 11 Bevans 946; 51 UNTS 233.]

and

Exchange of notes at Bern May 13, 1949, amending agreement of August 3, 1945.

Entered into force May 13, 1949

[63 Stat. 2437; TIAS 1929; 11 Bevans 960; 51 UNTS 129.]

* * *

AIR TRANSPORT SERVICES—MAY 13, 1949

ANNEX

* * *

SECTION VII

* * *

B. The rates to be charged by the air carriers of either contracting party between points in the territory of the United States and points in Swiss territory referred to in the attached Schedule shall, consistent with the provisions of the present Agreement and its Annex, be subject to the approval of the aeronautical authorities of the contracting parties, who shall act in accordance with their obligations under the present Annex, within the limits of their legal powers.

It is recognized that the determination of rates to be charged by an airline of one contracting party over a segment of the specified route, which segment lies between the territories of the other contracting party and a third country, is a complex question the over-all solution of which cannot be sought through consulation between only the two contracting parties. Pending the acceptance by both contracting parties of any multilateral agreement or recommendations with respect to such rates, the rates to be charged by the designated airlines of the two contracting parties over the route segment involved shall be set in the first instance by agreement between such airlines operating over such route segment, subject to the approval of the aeronautical authorities of the two contracting parties. In case such designated airlines cannot reach agreement or in case the aeronautical authorities of both contracting parties do not approve any rates set by such airlines, the question shall become the subject of consultation between the aeronautical authorities of the two contracting parties. In considering such rates the aeronautical authorities shall have regard particularly to Section IV of this Annex and to the desire of both contracting parties to foster and encourage the development of efficient and economically sound trunk air services by the designated airlines over the specified routes. If the aeronautical authorities cannot reach agreement, both contracting parties shall submit, at the request of either party the question in dispute to arbitration as provided for in Article 10 of the Agreement.

C. Any rate proposed by the airline or airlines of either contracting party shall be filed with the aeronautical authorities of both contracting parties at least thirty (30) days before the proposed date of introduction; provided that this period of thirty (30) days may be reduced in par-

ticular cases if so agreed by the aeronautical authorities of both contracting parties.

* * *

(3)

No. 86-998

In the Supreme Court of the United States

OCTOBER TERM, 1986

JAPAN AIR LINES COMPANY, LTD. ET AL., PETITIONERS

v.

ELIZABETH HANFORD DOLE,
SECRETARY OF TRANSPORTATION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

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Department of Justice
Washington, D.C. 20530
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13 pp

TABLE OF AUTHORITIES

Page

Cases:

Air Florida-BIA West Lease, 102 C.A.B. 730 (1983) 7

Airfreight Forwarders, Revocations, 65 C.A.B. 1605 (Bureau of Operating Rights 1974) 7

Air Tungaru-UTA, 90 C.A.B. 606 (1981) 7

Baltimore & O.S.R.R. v. *Settle*, 260 U.S. 166 (1922) 6

Canadian Colonial Airways, Inc.—Investigation, 2 C.A.B. 752 (1941) 7

Chevron U.S.A. Inc. v. *NRDC*, 467 U.S. 837 (1984) 6

Clarke v. *Securities Industry Ass'n*, No. 85-971 (Jan. 14, 1987) 6

Discount U.S.A. Fares, 48 C.A.B. 892 (1968) 9

Eastern Airlines, Inc., Enforcement Proceeding, 40 C.A.B. 745 (1964) 7

Qantas Empire Foreign Transfer Traffic Case, 29 C.A.B. 33 (1959) 4, 6

Resort Airlines Miami Stopover Investigation, 19 C.A.B. 1 (1954) 7

Sitmar Cruise Lines, 68 C.A.B. 1380 (1975) 6

Page

Cases—Continued:

Tariff Flexibility Rulemaking Proceeding, 46 Fed. Reg. 46787 (1981), aff'd mem. *sub nom. American Express Co.* v. *CAB*, 673 F.2d 550 (D.C. Cir. 1982) 6, 8

Texas & N.O.R.R. v. *Sabine Tram Co.*, 227 U.S. 111 (1913) 6

United States v. *Erie R.R.*, 280 U.S. 98 (1929) 6

Statutes:

Federal Aviation Act of 1958, 49 U.S.C. App. (& Supp. III) 1301-1552:

§ 101(10), 49 U.S.C. App. 1301(10) 2

§ 101(24), 49 U.S.C. App. 1301(24) 1

§ 403, 49 U.S.C. App. 1373 2

§ 1002, 49 U.S.C. App. 1482 2

§ 1002(k), 49 U.S.C. App. 1482(k) 2

§ 1102(a), 49 U.S.C. App. 1502(a) 2

§ 1601, 49 U.S.C. App. (& Supp. III) 1551 1

§ 1601(a)(2)(D), 49 U.S.C. App. 1551(a)(2)(D) 2

Miscellaneous:

Tariff Flexibility Rulemaking Proceeding, Order on Reconsideration, Order 81-11-58 (Nov. 10, 1981) 8

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioners contend that the Civil Aeronautics Board (CAB)[1] erred in determining that a cargo rate—the Export Inland Contract Rate (Ex/In Rate)—once offered by Northwest Airlines, Inc. (Northwest), for transportation between Chicago and Seattle was a rate offered in domestic rather than in foreign air transportation.

1. The Federal Aviation Act of 1958 (the Act), 49 U.S.C. App. (& Supp. III) 1301-1552, distinguishes domestic air transportation from "foreign air transportation" (49 U.S.C.

[1]The CAB's regulatory responsibilities were transferred to the Department of Transportation on January 1, 1985, pursuant to Section 1601 of the Federal Aviation Act of 1958, 49 U.S.C. App. (& Supp. III) 1551.

App. 1301(24), 1482(k)).[2] The classification of a fare or rate as one in "foreign air transportation" (generally referred to as an international fare or rate) is significant because international fares and rates must be filed in tariffs, and they are subject to review by the United States and by foreign governments.[3] By contrast, under Section 1601(a)(2)(D) of the Act, 49 U.S.C. App. 1551(a)(2)(D), fares and rates in domestic air transportation are no longer subject to government regulation.

The administrative proceedings in this case involved both the Ex/In Rate and certain "Visit USA" (VUSA) fares. The Ex/In Rate was offered for transportation of cargo between Chicago and Seattle but was only available for cargo destined for one of several specified points in Asia. The Ex/In Rate was offered without regard to the carrier used to transport the cargo between Seattle and Asia. Pet. App.

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[2]Domestic air transportation consists of "interstate" and "overseas" air transportation, the latter being limited to transportation between the United States and its Territories or possessions. Transportation that does not meet the definition of "interstate," "overseas," or "foreign" air transportation (such as a direct flight from one non-U.S. point to another) is not considered "air transportation" at all under the Act (49 U.S.C. App. 1301(10)).

[3]Section 403 of the Act, 49 U.S.C. App. 1373, requires the filing of international fares and rates in tariffs, and Section 1002 of the Act, 49 U.S.C. App. 1482, authorizes the Department of Transportation to investigate the lawfulness of international fares and rates. Section 1102(a) of the Act, 49 U.S.C. App. 1502(a), requires the Department to regulate air transportation in accordance "with any obligation assumed by the United States in any treaty, convention, or agreement" with another country. The international agreements relevant to this case give the Japanese and Swiss governments, respectively, the right to approve "[t]he rates to be charged by the airlines of either Contracting Party between points in the territory of the United States and points in the territory of Japan" (Pet. App. 161a-162a), and "[t]he rates to be charged by the air carriers of either contracting party between points in the territory of the United States and points in Swiss territory" (*id.* at 163a).

37a-38a. Petitioners, foreign air carriers whose fares and rates are generally subject to regulation by their governments, contended that the Ex/In Rate was international and therefore subject to foreign-government approval before being offered. Pet. App. 24a-26a. The VUSA fares were for passenger travel. Some VUSA fares, like the Ex/In Rate, are "unrestricted," and are available without regard to how the passenger travels between the foreign point and the United States. Other VUSA fares, however, are "restricted," *i.e.*, available only to traffic that uses specified carriers for transportation between the United States and the foreign point. Petitioners did not challenge the unrestricted VUSA fares in this proceeding but contended that the restricted VUSA fares were international. Pet. App. 30a-37a.

After an evidentiary hearing, an administrative law judge (ALJ) rejected petitioners' argument that a "flow of commerce" theory must be used to determine whether the rate or the fares were for foreign air transportation. The ALJ concluded instead that "[i]t is clear that the Board has not adopted the 'flow of commerce' theory as advocated by [petitioners]" (Pet. App. 111a). The ALJ recognized that the fares and rate were "novel" (*id.* at 116a). He found, however, that the fares and rate were "very close" to fares and rates that had historically been treated as international (*id.* at 120a), and he concluded that the Ex/In Rate and VUSA fares at issue should be classified as international (*id.* at 123a, 146a). The CAB reversed in part, holding that the Ex/In Rate was domestic; the CAB affirmed the conclusion that the restricted VUSA fares were international.[4] It

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[4]The CAB also addressed the status of unrestricted VUSA fares. Although no challenge to those fares was before it, the CAB thought it important, in light of the proper and unquestioned treatment of those fares as domestic, that its decision "adequately distinguish 'unrestricted' VUSA fares and make clear that the latter need not be filed" (Pet. App. 28a; see also Pet. App. 12a-13a n.3).

agreed that its precedent did not mandate the application of a flow-of-commerce test. The CAB explained that its historic practice had not been one of unquestioning reliance on flow-of-commerce analysis. Rather, "[w]here another test, such as a carrier's geographic operations, was more relevant to the statutory provision and policies at issue, flow of commerce principles were readily rejected." Pet. App. 56a (citing *Qantas Empire Foreign Transfer Traffic Case*, 29 C.A.B. 33 (1959)).

The CAB concluded that a carrier-restriction test should be used for determining whether the Ex/In rate and VUSA fares were domestic or international. This test "accord[s] with (1) economic reality [and] (2) competitive reality" (Pet. App. 29a) because if a "fare or rate is available on equal terms for sale by all willing participant carriers, there can be no doubt that it is economically independent of the international travel to which it is tied for marketing purposes. Put another way, the fare must stand on its own, competitively and economically, as a domestic fare." *Id.* at 64a. In addition, the CAB adopted its test to "strike a fair and reasonable balance between the competing, but legitimate, regulatory interests of both the U.S. and foreign governments" (*id.* at 63a).

Applying its test, the CAB determined that fares or rates such as the Ex/In Rate and the unrestricted VUSA fares, offered without regard to the international carrier used, would be treated as domestic fares or rates. By contrast, "carrier-restricted" fares or rates such as the restricted VUSA fares, which were available only to traffic that used specified international carriers, would be treated as international fares or rates. Pet. App. 63a-69a.

The court of appeals affirmed (Pet. App. 1a-22a). The court of appeals held that "[o]n its face the statute does not require that 'foreign air transportation' be defined by a

'flow of commerce' test" (*id.* at 9a). The court rejected petitioners' contention that the CAB was bound by its own precedent to follow a flow-of-commerce test, because "[i]t is apparent that the CAB has never stated that the 'flow of commerce' test is the *sole* test for determining whether air transportation is foreign" (*ibid.*). Rather, the court of appeals held that the CAB's "adoption of the 'carrier-restricted' test in this case was not a significant change from prior interpretations" (*id.* at 8a-9a). Accordingly, the court rejected petitioners' contention that "the agency has violated its obligation to interpret consistently the statutes under which it operates" (*id.* at 9a), and their argument that the principle of deference to an agency's interpretation of its organic statute was inapplicable (*id.* at 8a).

2. The decision of the court of appeals upholding the CAB's use of the carrier-restriction test is correct and does not conflict with any decision of this Court or any court of appeals. Accordingly, further review by this Court is not warranted.[5]

Petitioners contend that the CAB was bound to apply a flow-of-commerce test and to define the Ex/In Rate as international.[6] As the court of appeals noted (Pet. App. 9a), however, the statutory definition of "foreign air transportation" does not in terms require use of a flow-of-commerce test. Therefore, the court of appeals properly affirmed the

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[5]In addition to the substantive reasons for denying the petition, we note that Northwest charged the Ex/In Rate to only two shippers for a period of six months in 1981 (Pet. App. 37a), and Northwest has not used the rate since 1981. The tariff-filing status of a rate last charged over five years ago does not present an issue that warrants this Court's attention.

[6]Petitioners argue that " 'the essential character of the commerce' is the decisive test in resolving the status of a particular movement, * * * and that the shipper's [or passenger's] intent determines the essential character of the commerce" (Pet. 7 (citation omitted)).

CAB's decision that the Act permitted its use of the carrier-restriction test here. An agency's interpretation of its organic statute, of course, is entitled to substantial deference by a reviewing court if that interpretation is reasonable. See, *e.g.*, *Clarke* v. *Securities Industry Ass'n*, No. 85-971 (Jan. 14, 1987), slip op. 14-15; *Chevron U.S.A. Inc.* v. *NRDC*, 467 U.S. 837 (1984).

Petitioners argue (Pet. 11-13) that the CAB's choice of the carrier-restriction test is unreasonable, since it is assertedly inconsistent with numerous judicial and agency decisions that employed a flow-of-commerce test in interpreting other statutes. No court, however, has held that the Act's definition of "foreign air transportation" requires a flow-of-commerce test. By contrast, the CAB has consistently held that other criteria may be more appropriate "[w]here another test, such as a carrier's geographic operations, was more relevant to the statutory provision and policies at issue" (Pet. App. 56a, *quoted at* Pet. App. 11a). See also *Qantas Empire Foreign Transfer Traffic Case, supra; Tariff Flexibility Rulemaking Proceeding*, 46 Fed. Reg. 46787, 46792 (1981), aff'd mem. *sub nom. American Express Co.* v. *CAB*, 673 F.2d 550 (D.C. Cir. 1982); *Sitmar Cruise Lines*, 68 C.A.B. 1380 (1975).

This Court's decisions do not require application of a flow-of-commerce test. Petitioners rely on four cases[7] in which the Court determined that certain ground transportation was interstate rather than intrastate and that the ICC rather than state authorities had jurisdiction to regulate it. Those decisions construed statutes in which Congress had defined interstate transportation broadly so as to subject

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[7] *Texas & N.O.R.R.* v. *Sabine Tram Co.*, 227 U.S. 111 (1913); *Baltimore & O.S.R.R.* v. *Settle*, 260 U.S. 166 (1922); *United States* v. *Erie R.R.*, 280 U.S. 98 (1929); *United States* v. *Capital Transit Co.*, 325 U.S. 357 (1945).

the intrastate portion of interstate transportation to the comprehensive regulatory structure of the ICC. There is no reason to assume that Congress intended, in the Federal Aviation Act, to define "foreign air transportation" just as broadly so as to subject the domestic portion of international transportation to international proceedings rather than to Congress's own chosen regulatory (now, deregulatory) scheme.

In cases bearing no factual resemblance to the present case, the CAB has, to be sure, found some of those decisions helpful in distinguishing domestic from foreign air transportation,[8] and foreign air transportation from transportation that falls outside of the Act's provisions altogether.[9] Those CAB cases, however, all involved carrier-restricted travel, and there was no question in any of those cases about a carrier-restriction test. Those cases have no bearing on the question whether non-carrier-restricted travel should be deemed domestic or foreign.

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[8]*Resort Airlines Miami Stopover Investigation*, 19 C.A.B. 1 (1954) (carrier with only foreign and not domestic operating authority could offer stopovers in Miami only if they were of limited duration); *Eastern Airlines, Inc., Enforcement Proceeding*, 40 C.A.B. 745, 748 (1964) (carrier's offer of foreign rather than domestic fare for transport from U.S. points to Miami, based on brief sidetrip to Bahamas, raised "complex and novel legal issue" best dealt with through rulemaking); *Airfreight Forwarders, Revocations*, 65 C.A.B. 1605 (Bureau of Operating Rights 1974) (carrier could not avoid losing its domestic operating authority, on the basis of nonuse, just because its international shipments included transportation from one U.S. point to a U.S. gateway).

[9]*Canadian Colonial Airways, Inc.—Investigation*, 2 C.A.B. 752 (1941) (use of U.S. airspace and overnight stop in Jacksonville did not transform Canada-to-Bahamas trip into "foreign air transportation" subject to CAB jurisdiction; transportation was not "air transportation" at all within meaning of Act); *Air Tungaru-UTA*, 90 C.A.B. 606 (1981) (CAB had jurisdiction over entire U.S.-to-Tahiti route, including portion between Christmas Island and Tahiti flown by airline providing joint services with airline that flew U.S.-to-Christmas Island portion); *Air Florida-BIA Wet Lease*, 102 C.A.B. 730 (1983) (similar holding with respect to intra-European portion of continuous U.S.-to-Europe operation).

The CAB's decision here not to rely on a flow-of-commerce test is rational and consistent with past interpretations of "foreign air transportation." Application of a flow-of-commerce test under the Act could give foreign governments the power to review and disapprove fares and rates offered wholly within the United States. As the CAB observed in its *Tariff Flexibility Rulemaking Proceeding*, 46 Fed. Reg. at 46791-46792, the United States claims no such power to review fares and rates offered within foreign countries,[10] and a definition of foreign air transportation that would give foreign nations such a power over intra-U.S. fares and rates "is clearly at odds with the intent of the [Act]."[11]

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[10]"Our consistent practice has been to require the filing of foreign carriers' intra-border fares only to the extent that they are reflected in through or joint fares to U.S. points." 46 Fed. Reg. at 46791.

[11]Petitioners err in arguing (Pet. 17) that the *Tariff Flexibility Rulemaking* is not precedent for use of an alternative to a flow-of-commerce test. In that proceeding, the CAB held that fares for travel between U.S. points were domestic even though such fares could be combined with international fares for a through journey between a U.S. point and a foreign point. Petitioners contend that the CAB in fact applied the flow-of-commerce test in making this ruling, for the CAB (they say) merely recognized the "essential character" of these "combinable" fares as domestic. The CAB, however, in its order on reconsideration expressly considered—and rejected as "absurd"—a flow-of-commerce test focusing on passenger intent. As the CAB explained, if a passenger's intent were controlling, "so long as his itinerary included a foreign point, his entire journey would be in foreign air transportation," and the fare for any domestic segment included in such an itinerary would be subject to tariff-filing requirements as a foreign fare. *Tariff Flexibility Rulemaking Proceeding, Order on Reconsideration*, Order 81-11-58, at 2-4 (Nov. 10, 1981). The CAB affirmed its previous decision that fares that are merely combinable should be classified as domestic. Although the *Tariff Flexibility Rulemaking* is, as petitioners note (Pet. 17 n.9), distinguishable because it did not involve fares tied expressly to foreign transportation, the CAB correctly noted (Pet. App. 53a) that "there is nothing in the *Rulemaking* to suggest that the distinctions presented here by the marketing ties to foreign travel generally, or to particular carriers, necessarily requires [*sic*] a different result," *i.e.*, classification of the Ex/In Rate as international.

Moreover, even petitioners do not insist on the universal application of their flow-of-commerce test. VUSA-type fares without carrier restrictions have been offered by U.S. airlines since 1968. See *Discount U.S.A. Fares*, 48 C.A.B. 892 (1968). The CAB and foreign governments and carriers have considered them domestic (see Pet. App. 52a). Petitioners did not challenge the domestic status of the unrestricted VUSA fares before the agency (*id.* at 34a) or in the court of appeals. As the CAB observed, however, a flow-of-commerce test that focused on passenger intent would "render international * * * all VUSA fares" (*id.* at 56a).

b. Petitioners argue (Pet. 14-15) that the carrier-restriction test represents an unexplained departure from past agency practice. For reasons we have already discussed, and for additional reasons given by the court of appeals in its careful analysis of the issue (Pet. App. 9a-12a & n.2), petitioners are simply wrong.[12] The court of appeals correctly concluded that the CAB's adoption of the carrier-restriction test "was not a significant change from prior interpretations" (*id.* at 8a-9a).

In any event, the CAB provided detailed and economically sound explanations of why statutory policies did not support use of a flow-of-commerce test in this proceeding (Pet. App. 51a-63a) and of why it selected the carrier-restriction test (*id.* at 63a-67a). Petitioners offer no legal or economic analysis to challenge the CAB's conclusion, but only the ipse dixit that "[i]t is on its face unreasonable" to classify the Chicago-to-Seattle rate at issue here as domestic (Pet. 15). The CAB offered a more than sufficient explanation to overcome such a weak challenge on the merits.

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[12]Contrary to petitioners' suggestion (Pet. 16-17), the court of appeals correctly understood their flow-of-commerce test as focusing on "the 'essential character of the movement' " (Pet. App. 7a-8a) and rejected the test on that basis.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

CHARLES FRIED
Solicitor General

FEBRUARY 1987